wiley

ARTICLE

Four More Lessons for Product Stewardship "Visible Fee" Advocates from the California Carpet Experience

March 14, 2019

Article in Brief

Product stewardship programs intended to divert used consumer products from certain waste streams are on the rise worldwide and there are lessons to be learned from programs already in operation. This article provides an update to our January 2017 article, "California Carpet Experience Shows 'Visible Fees' May Not Be the Product Stewardship Panacea," and assesses the potential limitations and conflicts that can arise along the way. Consumer product manufacturers, suppliers, and recyclers should take note.

Introduction

California's used synthetic carpet recycling program mandate has been in place since 2010. The controlling legislation allows manufacturers to add a "visible fee" to carpet sold in the state. It initially was seen by some as a favorable solution to the question of how to finance stewardship efforts. But by January 2017, implementers faced major challenges to the continuation of their program, and thus to their ability to sell carpet in the nation's largest state by gross domestic product.

Wiley Rein's product stewardship experts at that time circulated an article addressing the situation. It was entitled "California Carpet Experience Shows 'Visible Fees' May Not Be the Product Stewardship Panacea."[1] In the two years since, there has been considerable conflict and controversy over the future of the state's carpet stewardship program, involving extensive regulatory interactions,

Authors

David B. Weinberg
Senior Counsel
202.719.7102
dweinberg@wiley.law

Practice Areas

Environment & Product Regulation

pursuit by regulators of a still-pending enforcement action,[2] and also new legislation.[3]

Last month, much of that conflict was resolved with CalRecycle's approval of a new Chapter O to previously only conditionally approved California Carpet Stewardship Plan 2018-2022 (Plan).[4] The 406-page Plan serves as yet another reminder of challenges facing those who are considering "visible fee" approaches to financing steward programs affecting other products.

We explain below four big lessons from this controversy and the resulting now-fully-approved 2018-2022 Plan. First, however, we provide a bit more background and context.

Background

The last several decades have seen a number of state and municipal mandates aimed at diverting used consumer products from landfills and incinerators, encouraging material recovery, and, especially in the case of plastic bag bans and "bottle bills," avoidance of littering.

Requiring retail consumers to pay a deposit or other "visible fees" when they purchase a product has been successful in several jurisdictions in maximizing the recovery of some types of used products: containers, lead batteries, TVs and similar electronic products, and consumer batteries, among other materials. Nonetheless, proponents of consumer product stewardship laws typically prefer schemes that impose on what they describe as product "producers" the burden of establishing programs to collect, handle, and recover constituents of products after the end of their useful lives, and also leave it to those "producers" to bear the program costs. The proponents argue that such "producer responsibility" mandates are an efficient way to discourage the incorporation of toxic constituents and excessive material in the covered products and to minimize product wastage. The goal is summarized with the catchphrase "design for the environment."

But proponents rarely give weight to a number of other realities that complicate the "producer responsibility" approach. These include the facts that many products contain separately manufactured components, complex world-wide supply chains that make it hard to identify the overall "producer" to whom to assign burdens, competitive pressures (especially from foreign companies), consumer demand for low prices, the absence of state jurisdiction over many product manufacturers, and the lack of even-handed and aggressive governmental enforcement. Combined, these often make the "producer responsibility" approach inequitable.

Faced with these realities, industries willing to accept the significant burden of operating post-use stewardship programs often look for other ways to fund those efforts. Imposition of "visible fees" on the sale of covered products often seems to be a fairer way to share program costs. This approach continues to leave some segment of the supply chain responsible for operating stewardship programs, which can be a very complicated exercise and carry with it potential for substantial liabilities. But it assures that a share of program costs are paid in connection with every covered product sold, wherever the manufacturer, no matter how complex the supply chain, while imposing minimal enforcement obligations on government and regardless of the vigor of enforcement. It thus reduces the competitive penalty accepted by suppliers who are prepared to act responsibly but must still compete with those who do not.

Furthermore, the success of several U.S. states and Canadian provinces with visible fees for various used products has shown that such a system can be workable. But implementing a "visible fee" system also presents its own challenges, as the California carpet experience demonstrates.

The California Carpet Experience

California first enacted a carpet stewardship statute in 2010 by way of AB 2398. It aimed to "increase the amount of postconsumer carpet that is diverted from landfills and recycled into secondary products" by "working to the extent feasible with the carpet industry and related reclamation entities."[5] Significant amendments to the statute were made in 2017, via AB 1158. The law is now codified as Chapter 20 of the California Public Resources Code.

This is a complex statute, and it is impossible to fully describe it in this brief update. But here are the key elements of the scheme as initially enacted:

- As enacted in 2010, AB 2398 required that carpet manufacturers establish stewardship programs that would increase recycling, recyclability, and diversion of synthetic carpet (nylon, PET, etc.) by "incentivizing the market growth of secondary products made from postconsumer carpet,"[6] complying "with [California's] solid waste management hierarchy,"[7] and providing education and outreach to "consumers, commercial building owners, carpet installation contractors, and retailers,"[8] among other things. To demonstrate compliance with the statutory qualification scheme, a state agency – CalRecycle – would have to approve the plan and any amendments to it.[9]
- Manufacturers' program plans were to "demonstrate to the department that [they had] achieved continuous meaningful improvement in the rates of recycling and diversion of postconsumer carpet . . . and in meeting the other goals included in the organization plan . . . ."[10] This was to be done "to the extent feasible based on available technology and information" while at the same time "not [creating] an unfair advantage in the marketplace."[11] If the implementation of the program did not produce "continuous meaningful improvement in the rates of recycling...and meeting other goals" set forth in the approved plan, CalRecycle could seek significant penalties. And, if the program were deemed inadequate, sale in California of any of the carpet it covered would be unlawful.[12]
- What made this approach different from most "producer responsibility" schemes was that costs of plan implementation were not to be absorbed by some actor in the supply chain, but to be assessed directly on consumers through an assessment – a "visible fee" – on every square yard of carpet sold in California.[13] From July 2011 through December 2012, AB 2398 required that manufacturers assess consumers a charge of five cents ($0.05) per square yard.[14] Thereafter, the amount of the assessment could be increased to "be sufficient to meet, but not exceed, the anticipated costs of carrying out the plan."[15] Those funds would be remitted to support implementation of the approved manufacturers' program.

AB 2398 recognized the Carpet America Recovery Effort (CARE) as the sole approved carpet stewardship organization through at least April 1, 2015.[16] CARE's initial, five-year California stewardship plan was approved by CalRecycle in January 2012. But CARE's initial 2016 efforts to renew the plan were rejected,

although the program remained operating.

More on that in a moment. First, however, a bit more on the plan as it has been operating. Since 2011, collected fees in California have been used by CARE to support the physical diversion of used carpet from landfill disposal, as incentive payments and subsidies to increase the diversion and recycling rates, and as grants and loans. Substantial funds have been spent on education and other activities.

However, in 2014, the price of oil—the raw material for virgin synthetic carpet fiber—plunged. One result was the reduction in demand for recycled fiber (which must compete in price against virgin fiber in the marketplace). The subsidies available from CARE became insufficient to support continued investment in the construction or even the operation of recycling capacity. Diversion and recycling rates declined. To fund greater subsidies, the consumer fee was increased to $0.10 and then $0.20. In 2016, CARE proposed a fee increase to $0.25, but its plan was rejected. Among other things, CalRecycle pointed to the inadequacy of the projected sums to "support[] a nascent California carpet recycling industry struggling to stay in business"[17] and failure to include "other ideas to improve the market mechanisms in the program."[18]

In rejecting the proposed plan CalRecycle increased the pressure on CARE and the industry in general by calling for new legislation and by initiating a still-unresolved enforcement action against CARE for not meeting statutory obligations.[19] In 2017 the legislature passed, and the Governor signed the requested legislation, AB 1158.[20]

As amended by AB 1158, the manufacturer-managed plan (or plans, should there be more than one) is (are) to reach a 2020 recycling rate for post-consumer carpet of 24% and to include "quantifiable five year goals" for further increases in that rate.[21] The amended law also revised the obligations of plan(s) to include "goals for how . . . to do" such activities as incentivizing markets for products made from postconsumer carpet, increasing processor capacity and carpet recyclability, and specified that funds collected through the visible fee cover not only operational costs, but also (among other things) incentives for recycling carpet materials and grants for training installers about recycling carpet.[22]

As supplemented by the recently approved Chapter O, CARE's 2018-2022 Plan responds to these mandates. It also anticipates developing variable fees for different types of carpets, with an average assessment of $0.35 per square yard.[23]

Four Lessons from This Experience

The foregoing summary of the California law and experience underlines the importance of clear and, from the perspective of any affected industry sector, favorable identification of what is being demanded of industry stewards, and a clear definition of the discretion of regulators to expand those requirements. It also demonstrates four solid lessons for promoters of "visible fee" stewardship programs.

1. It is Critical to Consider the Potential Competitive Implications of Assessments and Take Them into Account.

As explained above, the California visible fee on carpet has increased dramatically in the last decade – from $0.05 to $0.35 per square yard. But the demand for synthetic carpet floor coverings is not inelastic – substitute products are available, including carpets made from other fibers, tile, wood and a variety of other flooring materials, when prices of carpet increase, consumers can turn to alternatives.

Moreover, although a cost increase of a few cents per square yard may not be dispositive for homeowners who are purchasing relatively small amounts of carpeting (although sometimes, of course, it is), even a small per square yard fee can generate huge, material cost increases faced by commercial construction and business enterprises when considering purchases of large volumes of floor coverings. And, those commercial enterprises are carpet suppliers' largest markets.

The original version of the California statute required that an approved plan meet statutory goals "to the extent feasible based on available technology and information"[24] and that the amount of assessments "not create and unfair advantage in the marketplace for one or more of the companies in the [plan implementation] organization."[25] The 2017 amendments removed the first of these requirements, replacing it with a feasibility requirement that an approved plan "shall" incorporate amendments recommended by a newly established advisory committee.[26] And regulators have not interpreted either of these requirements as obligating plans to avoid disadvantages of covered products over their competition. Nor has any affected party chosen to pursue challenges to the regulators' interpretation.

The 2018-2022 Plan documents show that raising the cost of carpet has had the foreseeable effect:

[T]here has been an accelerating decline of sale [of covered carpet] in California as compared to the other 49 states. From 2013 to 2017, the average annual sales decline in California was 4.5 times greater than that for the rest of the country. The cumulative decline in sales in California over this period is -10% as compared to -2% for the rest of the United States. Historically, every additional $0.05 per square yard in the assessment has resulted in approximately a 2% decline in annual carpet shipments to California. However, this sales decline has accelerated to 3% and 4% over the last two years, respectively, as the assessment climbed from $0.10 per square yard to $0.25 per square yard.[27]

It should be noted that this predictable reduction of carpet sales also threatens the viability of any stewardship program. Fewer sales ultimately will mean less total funding, unless fees are increased dramatically. And, eventually, there may be no more juice to squeeze from the lemon.

The lesson for those industries contemplating advocacy of visible fees is clear: consider seeking to include in any statutory mandate provisions that provide some protection against compelled product substitution or crippling of sales – for example, modification of goals and obligations where cost increases become too great. This is especially important where increasing prices might cause unintended effects. These could be environmental, as where a likely substitute is not regulated and a switch in usage could result in the same problem the stewardship program was intended to correct or, indeed, some other problem. Or they may be social, for example by injuring economically-disadvantaged population sectors, or encouraging foreign competition. In the carpet context, these impacts are evidenced either in increasing the cost of housing or

compelling the replacement of synthetic carpets (including carpets made from recycled fiber) with other flooring. But their replacements ultimately may create similar (or greater) landfill loadings.

2. Antitrust Protections Are Vital

All product stewardship statutes impose obligations on some segment of the supply chain to take actions that might be characterized as unlawful under antitrust and other pro-competition laws. Typically, these are obligations to share costs or subsidize some recyclers. Consequently, the statutes almost always include provisions that immunize program participants from such claims under state law.

But states do not have authority to statutorily ban potential plaintiffs from exercising rights granted by Federal law. Considerable precedent establishes that the only basis on which stewards can have confidence of protection against Federally-authorized claims of anti-competitive activities is if the state supervision of program planning and implementation is adequate to support invocation of the "state action exemption" in Federal antitrust law. This is not the place to address that exemption in detail, but the fundamental concept is that where state law compels activity that otherwise might be considered an antitrust violation, and the state has mandated and supervised that activity while recognizing the potential competitive impacts, antitrust damages cannot be obtained.[28]

A 2018 recommendation from the Advisory Committee set up by 2017's AB 1158 underlined the need for this type of protection. The Committee recommended that different levels of assessments be imposed based on differing face fiber types.[29] How to go about developing and implementing such "differential assessments" is the subject of considerable discussion in the CARE 2018-2022 plan.[30] Ultimately, implementation of such assessments likely will result in having an industry-controlled organization making and implementing decisions, and these no doubt will have competition-effecting results.

Moreover, in any such situation there will be both winners and losers. While it may be unlikely that any government agency would seek to challenge the Plan's outcome, the losers may. And their most viable potential weapon would be a suit for treble damages under the Federal antitrust laws.

The need to demonstrate substantial state supervision to support antitrust defenses is no doubt one reason for the extensive discussion in the new plan of forthcoming efforts to evaluate and develop a differential assessment system, and for pursuing those efforts with state involvement.[31] Any other industry contemplating support for a visible fee product stewardship funding mechanism should study those portions of the plan carefully. This issue will be particularly important if, as may be the case as to carpet in California, variable assessment approaches become attractive.

3. Statutory Descriptions of Plan Requirements Drives Potential Costs

A principal basis for the historic conflict between CARE and its industry sponsors, on the one hand, and CalRecycle, on the other, was a different interpretation of the demands of the 2010 statute. AB 2398 required establishment of an industry-operated program pursuant to a CalRecycle-approved plan, and that the plan "achieve the purposes" of the statute,[32] achieve "continuous meaningful improvement" in rates of recycling

and diversion,"[33] and include a series of specified goals, measures, and education and outreach elements.[34] But the statute left considerable room for dispute about the meaning of those requirements. (The referenced "purposes" of the statute, for example, were "to increase the amount of postconsumer carpet that is diverted from landfills and recycled into secondary products or otherwise managed in a manner that is consistent with the state's hierarchy for waste management practices."[35])

Disagreement about the details of those requirements underlay CalRecycle's rejection of CARE's original post-2016 plan just before publication of our January 2017 article. It also was the foundation for CalRecycle's enforcement action against CARE and, ultimately, the enactment of AB 1158. A key feature of those 2017 amendments was to overcome many of the ambiguities that existed in the original statute.

The clarifications were largely wins for proponents of more aggressive stewardship activities. As noted above, they set a goal for a 24% recycling rate by the end of 2019, and of increased rates "continually" thereafter.[36] They also included much more specific directions as to what actions the program should encompass. Beyond the requirements described previously in this article, for instance, the amendments specified that the collected funds should be sufficient to "carry out the plan, including the administrative, operational, and capital costs of the plan," payment of CalRecycle's full supervisory costs, and "incentive payments . . . including incentives or grants to state-approved apprenticeship programs."[37]

The 2018-2022 CARE plan responds to these directives. Almost a quarter of its text, for example, is devoted to "market development" activities. These are summarized as including:

- Subsidies for collector/sorters, processors, and manufacturers;
- Targeted grants for selected capital projects, research development, and testing; recycled product procurement; design; and reuse and collection;
- Other financial incentives as market conditions indicate;
- Technical assistance; and
- Promote education and collaboration of and among stakeholders regarding opportunities within the marketplace.[38]

The detail with which the plan sets forth the justifications and strategies for awarding these subsidies no doubt reflects not only the needs for good management and transparency to many stakeholders, but sensitivity to the antitrust concerns discussed above. Independently of that concern, however, they provide a lesson to any other industry contemplating advocacy of a "visible fee": depending upon the clarity which is statutorily provided for the use of those funds, very complex and expensive mechanisms for stewardship support may be in the offing.

4. Appropriate Metrics Must Be Identified

As amended, California's carpet recycling statute states a goal of achieving a 24% recycling rate by January 1, 2020, and the CARE plan targets a 27% rate by December 31, 2022.[39]

Anyone considering initiation of such requirements should recognize, defining recycling rates has long been a challenge, and assume that their new program is consistent with practical results. For example, some consider the recycling rate to be the percentage of material recovered divided by collections. Others would compare the of amount material recovered divided by the amount of material "available for collection." The former avoids the difficult process of calculating "available" material, but also produces a higher percentage rate.

Yet the difficulty of making necessary calculations cannot be overstated. For example, calculating the recycling rate for plastic soda pop bottles would seem to be simple: common sense says sales are almost equivalent to material available for collection, so the divisor should be "easily" calculated. And, collections may be determinable: discards are typically palletized and shipped for processing. But what is the numerator. Is the weight of that palletized material the proper numerator? Or is the weight of reusable plastic pellets generated from processing the collected material the correct measure? And, if the latter, how does one determine that amount, especially if much of the recovery is occurring in China or elsewhere outside U.S. boundaries?

The calculation becomes even more complex with long lasting products. Consider the calculation of the lead recycling rate of lead batteries. Millions of lead batteries are sold in the U.S. annually, for a variety of purposes. (The largest is for starting internal combustion engines, but these batteries also play a major role in providing motive power and power storage.) But depending on the use to which each is put, not to mention weather conditions, product lifetime varies.

Fortunately, reliable data has been collected for years on the average life of each type of battery, the average weight of lead in each type of battery, the output of recycling facilities (secondary smelters), the exports of used batteries for recycling, and imports of new batteries and lead ingots. So, by looking back the appropriate number of years for sales at that time and applying the appropriate average life expectancy of each type of battery, and totaling annual recycled lead production, adjusting for imports and exports, one can get a reliable estimate of batteries available for recycling in any year and the lead produced from them. The rigorousness of this process has allowed US EPA to repeatedly recognize the accuracy of the calculated 99% recycling rate for battery lead.[40]

But such data is often not available as to other products. Carpet provides a good example. The definition applicable to the CARE plan is "the proportion of carpet discards converted into recycled output, expressed as a percentage of carpet discards.[41] But making this calculation requires complex analyses. Calculation of annual discards requires consideration of historic sales, typical replacement rates, and the average carpet weight per square yard, among other things.[42] Similarly, calculating recycled output requires collecting information on a variety of reusable materials, including fiber, shredded carpet tile, depolymerized chemical components, and others.[43] The 2018-2022 Plan addresses these matters and sets forth measurement mechanisms and calculation formulae. But it also acknowledges that CalRecycle has employed a different calculation and commits to working with CalRecycle to resolve the differences.[44]

The lesson for those considering tying the amount of a "visible fee" to recycling rates: be thoughtful as to how the calculation of the target rate is to be made. And make sure the statute defines metrics in a way consistent with available or readily collectable information and minimizes the risk that inappropriate metrics could be

imposed.

---

[1] The Update is available at https://www.wileyrein.com/newsroom-newsletters-item-California-Carpet-Experience-Shows-Visible-Fees-May-Not-Be-the-Product-Stewardship-Panacea.html.

[2] Carpet America Recovery Effort, OAH No. 2017040578, Agency No. 2017-001-CARPET (2018).

[3] 2017 Cal. Legis. Serv. Ch. 794 (AB 1158).

[4] Available at https://www2.calrecycle.ca.gov/PublicNotices/Details/3572.

[5] 2010 Cal. Legis. Serv. Ch. 681 (AB 2398) § 1(f).

[6] Cal. Pub. Res. Code § 42972(a)(2).

[7] *Id.* § 42972(a)(3).

[8] *Id.* § 42972(a)(5).

[9] *Id.* § 42973.

[10] *Id.* § 42975(a).

[11] *Id.* § 42972(a)(6)(c)(2) (initial plan); *Id.* § 42973(a)(2)(B) (Plans after April 1,

2015).

[12] 2010 Cal. Legis. Serv. Ch. 681 (AB 2398) § 1.

[13] *Id.*

[14] *Id.* § 42972.5.

[15] *Id.* § 42972(a)(6)(c)(2).

[16] *Id.* § 42971(e)(2).

[17] Memorandum from Howard Levenson to Scott Smithline re Consideration for Approval of

California Carpet Stewardship, p. 3.

[18] *Id.* at 4.

[19] Carpet America Recovery Effort, OAH No. 2017040578, Agency No. 2017-001-CARPET (2018).

[20] 2017 Cal. Legis. Serv. Ch. 794 (AB 1158).

[21] Amended 42972(a)(2).

[22] *Id.*

[23] Plan, p. 171.

[24] Cal. Pub. Res. Code § 42972(a)(2).

[25] *Id.* § 42973(a)(2)(B).

[26] *Id.* § 42972.1(c).

[27] Plan, p. 171.

[28] *See e.g.*, Federal Trade Comm'n v. Phoebe Putney Health System, Inc., 568 U.S. 216 (2013).

[29] Plan, Att. 5, pp. 290-92.

[30] E.g., Plan, pp. 174-187, App 9; App 10.

[31] E.g., Plan, pp. 171-187.

[32] Cal. Pub. Res. Code § 42972(a)(1).

[33] *Id.* § 42957(a).

[34] *Id.* § 42972(a)(2)-(6).

[35] *Id.* § 42970.

[36] *Id.* § 42972.2.

[37] *Id.* § 42972(a)(4).

[38] Plan, p. 109.

[39] Plan, p. 25.

[40] Available at https://www.epa.gov/facts-and-figures-about-materials-waste-and-recycling/advancing-sustainable-materials-management.

[41] Plan, p. 247.

[42] *Id*, at 27-28.

[43] *Id*. at 247.

[44] *Id*. at 28.