



The City of San Diego

Staff Report

DATE ISSUED: September 4, 2018

TO: City Council

FROM: Environmental Services Department

SUBJECT: Seventh Amendment to Curbside Materials Processing & Marketing Contract with IMS Recycling Services and Allan Company

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Council District(s): All

OVERVIEW:

This action authorizes a Seventh Amendment to the City's Curbside Recyclable Materials Processing & Marketing Contract. This proposed amendment will modify the Compensation and Payment Schedule of the agreement with IMS Recycling Services and Allan Company for curbside materials processing to adjust for significant operational and cost impacts resulting from unprecedented changes in the recycling market.

PROPOSED ACTIONS:

A Resolution authorizing the Mayor, or his designee, to execute a Seventh Amendment to the agreement with IMS Recycling Services and Allan Company for processing, transporting and marketing commingled curbside recyclables.

DISCUSSION OF ITEM:

The Environment Services Department (ESD) offers single stream automated collection to approximately 255,000 City residences on a bi-weekly schedule. On December 14, 1998, through a competitive process, the City awarded a contract to IMS Recycling Services and Allan Company (collectively "Contractor") for processing, transporting and marketing the curbside recyclable materials that City forces collect from residents and deliver to the Contractor. The current term of the contract, which does not have any remaining extension options, ends on June 30, 2019.

A provision in this contract, Section 3.0, subsection 3.15 Increases Related to Regulatory and/or Legislative Initiatives, obligates the City to meet and confer with the Contractor, in good faith, to discuss adjustments to the contract's Compensation and Payment Schedule due to material and adverse changes in Contractor's operating or processing costs resulting from an event or change beyond the reasonable control of the Contractor.

The Contractor, as has the industry in general, has been significantly negatively impacted by the effects of China's National Sword Policy (Policy). Historically, China has been the largest international consumer of recycled materials. CalRecycle estimates that one-third of recyclable material generated in California annually is exported to foreign markets, of which, 62 percent is sent to China. In 2017, recyclable materials exported from California had a total value of approximately \$5.2 billion.

China announced a National Sword Policy in July 2017 which became effective March 1, 2018. The Policy banned the importation of certain recyclable commodities, particularly mixed paper, plastics, and metals; imposed unprecedented lower allowances for contaminants that are much stricter than international standards; significantly cut back on the import volume; and increased inspections of recyclable commodity imports.

The Policy has adversely led to a surplus of available United States material, sharp declines in pricing, and a lack of markets for the materials. For a material that now has lower value, material recovery facilities (MRF), which process and sort collected recyclable materials, are having to spend more money and resources to hire

workers and slow down sorting lines to meet the higher quality standards, and stockpile material for longer periods of time until material is sold to avoid disposing it in the landfill.

On May 4, 2018, China further expanded the Policy by suspending imports of any recyclable materials from the United States for one month. This suspension aggravated the situation by completely banning the few remaining recyclable commodities, including cardboard, which were still being shipped to China, and creating more price uncertainties. In June, China did re-open its doors to accept cardboard from the United States at the 0.5 percent contamination allowance and subject to multiple required inspections, one pre-shipment inspection at the recycling facility and again once at Chinese ports. Currently, there are very few inspectors in California to perform the pre-shipment inspections, resulting in very limited opportunity to send any cardboard to China.

Historically, about 80% of the City's curbside material is exported via the City's Contractor. In the first quarter of CY 2017, approximately 60% of the exported material (by weight) went to China and 40% went to other countries worldwide. During the first quarter of CY 2018, approximately 24% of the exported material (by weight) went to China and 76% went to other countries. This situation has already impacted revenue. In FY 2017, revenue to the City was \$4.0 million and in FY 2018, revenue was \$3.0 million.

At the Contractor's request, ESD staff met with the Contractor to discuss some relief for the cost impacts created by the unprecedented events resulting from China's National Sword Policy. To ensure that the City's material, including residual plastics, continues to be recycled, and in consideration for prioritizing the City's material, certain aspects of the financial terms of the contract will be adjusted. The financial terms of the contract that make up the City's revenue include a guaranteed floor price, a guaranteed \$6 per ton in revenue sharing, and a 50%/50% revenue sharing provision. Retroactive to May 1, 2018, the guaranteed floor price and the \$6 per ton in guaranteed revenue will be suspended. The City will potentially continue to receive revenue from the 50%/50% revenue sharing provision, which will be modified in such a way that any revenue for the City will cover the costs for recycling and transporting residual plastics. Monthly, any revenue for the City will be first allocated to pay the costs for the recycling and transporting residual plastics. The revenue balance, if any, will be the net revenue paid to the City. In the months in which costs exceed revenue, Contractor will pay for the costs for recycling and transporting residual plastics and note a credit to be deducted in future months in which the City has positive revenue. If at the end of the contract on June 30, 2019 there is a balance, the Contractor will not seek payment and the balance will be erased.

The need for increased quality and shift in market locations resulting from China's National Sword Policy on the recycling market are expected to be permanent and reflected in the responses to the Request for Proposals (RFP) for the next recyclable material processing contract. These changes may result in shifting the terms of the next contract from a revenue contract to a cost contract.

City Strategic Plan Goal(s)/Objective(s):

Goal 3: Create and sustain a resilient and economically prosperous City

Objective 4: Prepare and respond to climate change

Objective 5: Enhance San Diego's global standing

Goal 2: Work in partnership with all of our communities to achieve safe and livable neighborhoods

Objective 4: Foster services that improve quality of life

Fiscal Considerations:

Revenues to the City's Recycling Fund from the sale of recyclable commodities under this contract generated \$3.0 million in FY 2018. If the amendment is approved, the City's revenue under the contract would decrease by at least \$1.5 million for FY 2019 due to the suspension of guaranteed revenues. The Recycling Fund is positioned to absorb the decrease in revenue and continue providing the same level of service. Given the uncertainties of the recycling markets, at this time, it is not possible to predict how much the commodity prices will continue to decline but it is anticipated that the impact will be greater, and therefore \$0.00 revenue is forecasted for FY 2019. However, conservative changes in commodity prices, could potentially result in some revenue.

Environmental Impact:

This activity is not a "project" pursuant to CEQA Guidelines Section 15378(b)(4) and is therefore not subject to the California Environmental Quality Act (CEQA) pursuant to CEQA Guidelines section 15060(c)(3).

Equal Opportunity Contracting Information (if applicable):

This agreement is subject to the City's Equal Employment Opportunity Outreach Program (San Diego Ordinance

No. 18173, Sections 22.2701 through 22.2708) and Non-Discrimination in Contracting Ordinance (San Diego Municipal Code Sections 22.3501 through 22.3517).

Previous Council and/or Committee Actions:

On January 31, 2018, with Resolution R-311510, Council approved execution of the sixth amendment to the Curbside Recyclable Materials Processing & Marketing Contract with IMS Recycling Services and Allan Company to adjust revenue sharing provisions in order to address Contractor's material and adverse operating cost increases due to mandatory State and local minimum wage increases.

On May 24, 2018, ESD staff prepared a memorandum for Council to provide an update on China's National Sword policy impact on the City of San Diego's curbside recycling program, and of an upcoming amendment to the contract to address the Contractor's request for relief.

This item was heard at the September 13, 2018 Environment committee.

Key Stakeholders and Community Outreach Efforts:

Key stakeholders include City of San Diego residents, IMS Recycling Services and Allan Company.

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Environmental Services Department Director

Johnnie Perkins

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