City of Raleigh

NORTH CAROLINA

INTEROFFICE MEMORANDUM

DATE: June 27, 2016

TO: Ruffin Hall, City Manager
Tansy Hayward, Assistant City Manager

FROM: Fred Battle, Solid Waste Services Director

CC: David Scarborough, Assistant Director, Solid Waste Services
Andrew Martin, Assistant Director, Solid Waste Services
Charles Jackson, Budget Analyst, Solid Waste Services

SUBJECT: Sonoco Contract Modification

Effective July 1, 2006, the City entered into an agreement with Sonoco Recycling (Sonoco) for the processing and marketing of recyclable materials. This agreement was originally set to expire June 30, 2011, but was amended in 2008 and 2011. The current contract provides a fixed rate of $30 per ton for residential commingled materials, and will expire June 30, 2016. The current agreement allows the City two one- year extensions with the current price model.

In 2015, Sonoco management approached the City in regards to modifying the existing contract due in part to a decline in recycling sales and financial challenges faced by the local material recovery facility. On March 31, 2016, the City and Sonoco agreed in principle to modify the terms of the contract with a commitment to an additional five years at the end of the existing contract; Sonoco was advised that any changes would require administrative and City Council approval. The modification offers an adjusted rate of $9 per ton for recyclable materials, with a weighted average price (WAP) between $70 and $90 per ton. In the event the WAP for the recyclable materials amount to less than $48 per ton, the City will be charged a dollar for dollar ($1 to $1) surcharge for each decrease in the WAP amount.

Staff completed an analysis comparing options which include modifying the existing contract, extending the existing contract, or establishing a competitive bid for the City's recyclable materials. This analysis required an in-depth understanding of: 1) price volatility in recycling markets; 2) operational impact to the recycling program; and, 3) the fiscal impact to the Solid Waste Enterprise Fund. This memo provides a summation of staff findings, which address these factors to support the recommendation to the City Council.

Price volatility

Price volatility in recycling markets is a given. Prices for all recycled materials tend to follow expansions and contractions in overall demand for manufactured goods. At the same time, specific trends in each industry - be it paper/paperboard, glass, aluminum, or plastics - can push prices for different recycled materials in opposite directions. The aggregate of these prices has a direct effect on the WAP for recyclable material. Table 1 shows Sonoco's WAP over a ten-year period. Carefully negotiating long-term contracts that feature price floors or other revenue/risk sharing agreements can moderate revenue peaks and valleys. Staff has identified a wide range of proposals which consider the need to mitigate the City's exposure to surcharges while leveraging opportunities for revenue growth. Table 2 provides a list of proposals of estimated revenues and charges.

Proposal D is the recommended option. It balances the potential for revenue growth if market conditions improve while minimizing exposure to floor base charges. Based on the World Bank commodity forecasts, the City can (at least) expect a budget-neutral impact as a result of market volatility. As Table 3 below indicates, the forecast for crude oil (which impacts recycling prices) reveals an expected increase in crude oil prices for the next decade. The $48 per ton floor-base in Proposal D guards against potential financial risk as crude oil prices are expected to rise. Also, efforts to prohibit additional charges for glass processing offsets any floor base charges in the event of a market decline. The totality of each of these factors provides the rationale for selecting Proposal D.

Operational Impact

Another challenge for staff was to examine the operational or business impact caused by a potential change of recycling vendor. Major issues include: a) changes in existing collection routes; and b) possible changes in the recycling materials collected. A brief summation of each is provided below.

Changes in existing collection routes. In order to address location of new materials recovery facility, current recycling routes might need to be adjusted or completely rerouted. This could result in service day changes, adding of collection routes, or service delays due to extended collection routes.

Additional collection routes result in a greater risk for accidents, injuries to the public and staff, as well as a shorter vehicle useful life. Each of these risks presents significant threats to the department.

Changes in recyclables. Agreeing to terms on acceptable materials with a new recycling vendor may require substantial changes to recycling program operations. Even minimal changes to the recycling stream can add difficulty in managing staffing and capital equipment. For example, additional code enforcement positions would be required to ensure compliance with changes in acceptable recyclable materials being introduced into the material stream.

Fiscal Impact

Perhaps the greatest benefit of extending the existing Sonoco contract involves maintaining the City's fiscal soundness of operating the recycling program. This includes avoiding excessive recycling processing fees and controlling operational costs.

Excessive Fees. There are many disadvantages of soliciting requests for proposals in the present recycling market. Many recycling companies have closed material recovery facilities due to the prolonged downturn in the recycling market. As a result, many municipalities no longer have the contractual leverage enjoyed in recent years, and are incurring processing fees for glass and other materials that previously represented a revenue source. Other costs include floor-base charges when the WAP falls below a specific threshold amount. There are substantiated reports of municipalities incurring floor-base charges as high as $60 per ton as new agreements are entered into with vendors. As a result, these municipal budgets are hit with unplanned expenditures which were unanticipated before the recent market decline.

Controlling Operational Costs. The City also faces the risk of increasing operational costs as a result of bidding its recyclables on the open market. Such factors include higher fuel and maintenance costs due to hauling both recycling materials and residuals at further distances. In addition to increased cost for direct materials, SWS would likely pay higher labor costs, to include overtime, temporary staffing or an increase in full-time staff needed to meet these operational changes.

Final Recommendation

It is in the City's best interest to extend the existing recycling contract as bidding in the current market presents greater economic, operational, and fiscal risks. As Table-3 shows, market conditions indicate minimal increases to the price of recycling materials over the next five (5) years. Therefore a 3-5 year term would provide a clearer picture of market changes and define the necessary course of action.

Table1. Sonoco Recycling Weighted Average Price (2007-2015)

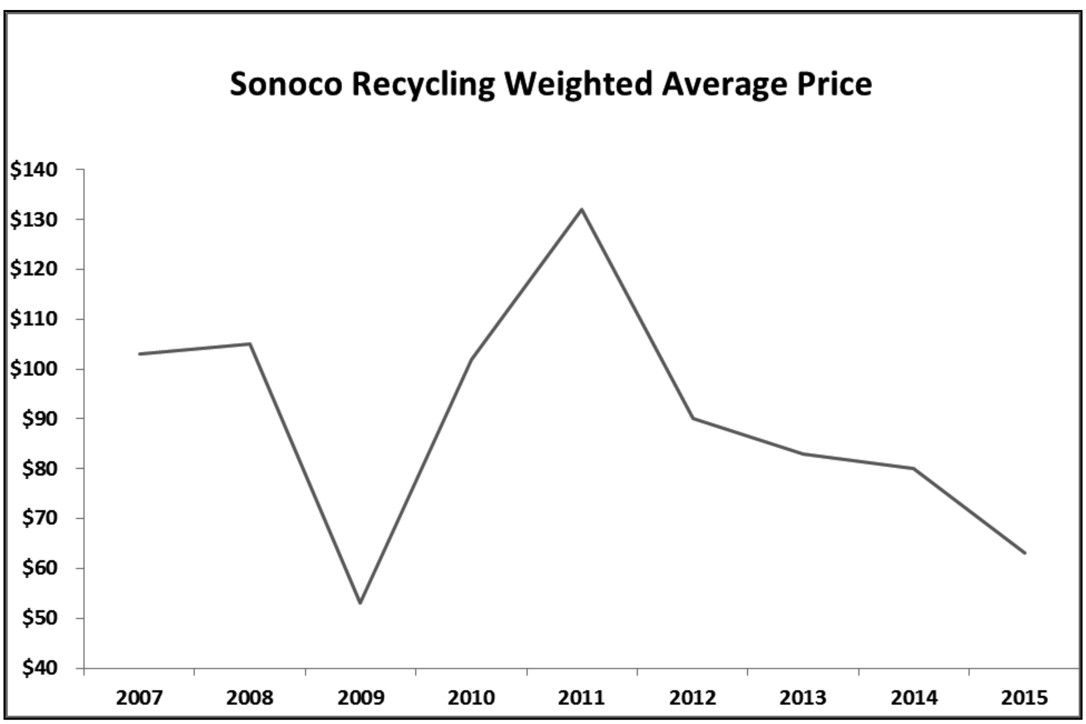

Table2. Schedule of Estimated Revenues by Proposal

Weighted Avg Price	Proposal A ($17 per ton)	Proposal B ($5 per ton)	Proposal C ($10 per ton)	Proposal D ($9 per ton)
Above $70-$90 per ton	$510,000 + 50% revenue	$150,000 + 50% revenue	$300,000 + 50% revenue	$270,000 + 50% revenue
$70-$90 per ton	$510,000	$150,000	$300,000	$270,000
$69 per ton	$480,000	$120,000	$270,000	$240,000
$68 per ton	$450,000	$90,000	$240,000	$210,000
$67 per ton	$420,000	$60,000	$210,000	$180,000
$66 per ton	$390,000	$30,000	$180,000	$150,000
$65 per ton	$360,000	$0	$150,000	$120,000
$64per ton	$330,000	$0	$120,000	$90,000
$63 per ton	$300,000	$0	$90,000	$60,000
$63per ton	$270,000	$0	$60,000	$30,000
$62per ton	$240,000	$0	$30,000	$0
$61 per ton	$210,000	$0	$0	$0
*$60 per ton	$180,000	$0	$0	$0
$59 per ton	$150,000	$0	$0	$0
$58 per ton	$120,000	$0	$0	$0
$57 per ton	$90,000	$0	$0	$0
$56 per ton	$60,000	$0	$0	$0
$55 per ton	$30,000	$0	$0	$0
$54 per ton	$0	$0	$0	$0
$53 per ton	$0	$0	$0	$0
$52 per ton	**1-for-1 Dollar charge**	$0	$0	$0
$51 per ton	**1-for-1 Dollar charge**	$0	$0	$0
$50 per ton	**1-for-1 Dollar charge**	$0	$0	$0
$49 per ton	**1-for-1 Dollar charge**	$0	$0	$0
$48 per ton	**1-for-1 Dollar charge**	$0	$0	$0
$47 per ton	**1-for-1 Dollar charge**	$0	$0	**1-for-1 Dollar charge**
$46 per ton	**1-for-1 Dollar charge**	$0	$0	**1-for-1 Dollar charge**
$45 per ton	**1-for-1 Dollar charge**	$0	$0	**1-for-1 Dollar charge**
Less than $45 per ton	**1-for-1 Dollar charge**	$0	**1-for-1 Dollar charge**	**1-for-1 Dollar charge**

Table3. World Bank Commodity Forecast price Data, January 2016