

## Tips for Negotiating Municipal Recycling Contracts in a Changing Marketplace

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In a July, 2017 filing with the World Trade Organization, China's Ministry of Environmental Protection announced that the country would begin prohibiting the importation of some grades of recovered paper and plastic, the so-called "National Sword Policy". China began enforcing its importation policy in January 2018, banning certain materials and lowering the acceptable contamination rate to one-half of one percent for materials not banned. Since material recovery facilities in the United States achieve an average contamination rate of between three and five percent, according to [resource-recycling.com](http://resource-recycling.com), China's National Sword Policy is an effective ban on importation of recyclable materials from the United States.

The National Sword Policy has caused dramatic upheaval in the recyclable commodities market in the U.S., Massachusetts included, and it demonstrates the problem with relying so heavily on a single importer. The challenges may worsen, as China is now contemplating adding to the list of banned recovery materials. Domestic processing facilities are scrambling to find alternative buyers, particularly in Southeast Asian countries such as Thailand, Vietnam and Malaysia— although they, too, have begun restricting the amount of recovered material they are willing to import through similar contamination requirements.

While exporters struggle to find sufficient buyers in the current marketplace, a significant amount of material from Massachusetts is either being stockpiled or, in some cases, sent to landfills under Department of Environmental Protection waivers. Consequently, cities and towns in the Commonwealth are left bearing the financial impact through their contracts with vendors for the collection and disposal of recyclable materials.

### Contracting for Solid Waste and Recyclables in Current Climate

China's National Sword Policy may be the most extreme shock to the global marketplace for recycling materials, but it is neither the first nor will it be the last. As a result of the ever-changing global marketplace, and the overreliance of the U.S. on a single importer of materials, the days of contractors willing to offer a single per-ton cost for all recyclable materials over a long-term contract are likely over. Many municipalities in Massachusetts are now involved in disputes—in some cases, formal legal proceedings—to determine whether vendors have the right under their specific contracts to charge a higher rate for the collection and disposal of recyclables based on market condition changes.

China's policies highlight the importance of diligently negotiating collection and disposal contracts that are as favorable to the municipality as the marketplace will permit. For example, if a municipality agrees to include a change-in-law provision due to persistence from the vendor, the provision should be drafted narrowly and should

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exclude instances of changing market conditions, as opposed to actual local, state or federal regulation or legislation that directly impacts the provision of services under the agreement. Additionally, if there is a change-in-law provision, there also needs to be a provision that specifies a formula for how costs will be adjusted as a result of the change in law.

When a municipality chooses to enter into a long-term contract, it does so, at least in part, to lock in pricing. China's National Sword demonstrates how quickly and dramatically the market can change. Accordingly, it is generally advisable to keep contract terms to three years or fewer, because there is no telling in which direction the market may change, and municipalities do not want to be stuck in contracts where they are paying more than a neighboring community.

Municipalities can also consider a most-favored-nation-status clause, which will ensure that if the market returns, and the vendor's pricing at that time is more favorable than when the municipality executed the contract with the vendor, the contract will be amended to match the pricing the vendor is offering to other municipalities. A "re-opener" clause is another effective means of allowing the municipality to negotiate mid-contract and ensure that it shares in any cost savings that result from a positive change in the market for recycled materials.

Dramatic market shifts can threaten the existence of smaller vendors that do not have the financial resources of larger, national and international vendors in the industry. With this in mind, municipalities are advised to require a performance bond, which provides the assurance that the surety guaranteeing performance of the contract will be obligated to provide a replacement vendor to perform the services consistent with the contract that the municipality expended significant resources to negotiate. A performance bond is typically issued annually in an amount equal to the projected cost of the contract over a twelve-month period.

While these types of contracts are exempt from the public procurement requirements found in the Massachusetts Uniform Procurement Act, publicly bidding these contracts should, at least in theory, increase competition and result in a better price. A public procurement process also allows a municipality to specify the substantive terms and conditions that it will require the vendor to agree to if it wishes to perform the services. The procurement documents should also note that, while the community has elected to use a public process, it is not subject to the various statutory requirements found in the Massachusetts Uniform Procurement Act.

### **Long- and Short-Term Means of Alleviating Market Pressure**

As the cost to municipalities to collect and dispose of recycling begins to equal — and at times exceed — the cost of disposing of solid waste, there are going to be those who question the impetus of even trying to recycle any longer. The most glaring deficiency in this reaction is that it underestimates the extreme lack of capacity the Commonwealth is facing in the disposal of its solid waste. Producing more waste is simply not a sustainable solution to the problem in the global commodities market. While increased self-reliance is the clearest, most sustainable means of hedging the ever-changing global marketplace, developing additional local infrastructure capable of repurposing the materials would not address the problem in the near term. The process first requires willing, motivated investors, and then those investors need to embark on permitting, financing and constructing the facilities. It takes years before a facility is operational.

The reality is that educating the public and producing recyclable materials with less contamination is the most practical and realistic short-term solution to creating a more desirable commodity for potential buyers. Reducing contamination enhances the collection vendor's ability to find disposal facilities willing to accept the materials—and to accept them at a better rate—because it will increase the disposal facility's ability to find a buyer for the end material in this constricted and challenging market. Municipalities, through contracts that were carefully negotiated with the assistance of municipal counsel, will then share in those savings.

Please contact Attorney John W. Giorgio ([jgiorgio@k-plaw.com](mailto:jgiorgio@k-plaw.com)) or any other attorney in our Contracts and Procurement Practice Group at 617-556-0007 with further questions.

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