

Mid-Term Review of Revised Environmental Handling Fees for Phase I Regulated Electronics

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Commissioned by:



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1.0 INTRODUCTION

1.1 BACKGROUND AND OBJECTIVES

In August 2009 ACES, ESABC, and SWEEP implemented revised environmental handling fees (EHFs) on Phase I regulated products (desktop computers, laptop computers, display devices, desktop printers and fax machines, and computer peripherals). These revised fees (and product categories) reflected the recommendations of the Phase I report commissioned by the three programs.¹ The report recognized that the assumptions and estimates used to calculate the EHFs, while conservative and reasonable, would need to be reviewed for reasonableness in consideration of actual operating costs, collection rates, and product sales. Therefore the Phase I report recommended that ACES, ESABC, and SWEEP conduct a high-level review of the Phase I EHFs at a pre-determined interval.

The current study was undertaken as follow-up to the 2009 Phase I report. The study was conducted by InterGroup in close coordination with the EHF Review Advisory Committee (hereafter, "Advisory Committee"). The Committee consisted of personnel representing the following organizations:

- Resource Recovery Fund Board (program manager for ACES);
- Encorp Pacific (program manager for ESABC);
- Product Care Association (program manager for SWEEP);
- Alberta Recycling Management Authority (ARMA);
- Ontario Electronic Stewardship (OES); and
- Director, Harmonization ACES, ESABC, and SWEEP.

The objectives of this exercise were as follows:

- In a manner consistent with program fee-setting principles and methods, develop an approach that could be used to evaluate the extent to which the revised Phase I EHFs (and, in the future, Phase II EHFs) contribute to a viable and sustainable program: specifically, to find a balance between collecting enough revenue to cover program expenses and allocate funds for special purposes, like the operating contingency reserve (OCR) and Effectiveness and Efficiency (E & E) Fund, while not accumulating excess reserves.
- Determine an indicator (or a set of indicators) that could be used to identify any material problems related to revenue over-collection or under-collection and to ascertain if the EHFs are reasonable. This may relate to specific product categories and/or the program as a whole.
- Help to develop a process for monitoring and evaluating the fees that have been implemented.

¹ InterGroup Consultants and Forkast Consulting. 2009. Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada – Calculation of Revised Environmental Handling Fees for Phase I Products.

1.2 METHODOLOGY IN BRIEF

Kick-off Call - A kick-off conference call with the Advisory Committee was conducted to clarify and confirm study objectives, schedules, and participants and to discuss a preliminary approach for evaluating the revised EHF's.

Program-specific Calls - A series of telephone calls with each program were undertaken to gain relevant information and insight into specific programs, including defining a threshold, actions to take once a threshold has been exceeded, and other administrative considerations (see Appendix A).

Initial Perspectives and Recommendations - InterGroup subsequently devised a set of initial perspectives and recommendations intended to summarize the key findings of the research and provide options for the programs to consider.

Web Conference - InterGroup and the Advisory Committee engaged in a web conference to review key findings from the research to date, agree upon a set of guiding principles for evaluating and monitoring EHF's, and discuss potential indicators and process considerations.

Follow-up Call - A follow up conference call with the Advisory Committee was conducted to discuss findings from the web conference, in particular, feedback regarding guiding principles, a process flow chart, and the OCR.

Documentation - A draft technical memo was circulated to Advisory Committee members as well as each program's Executive Director for review. The technical memo was revised based on comments from this review process.

2.0 MONITORING/EVALUATING EHF's

2.1 GUIDING PRINCIPLES

Based on discussions with the Advisory Committee, a set of Guiding Principles for Monitoring and Evaluating EHF's was developed. These principles were intended to guide the assessment and selection of monitoring and evaluating indicators and are generally consistent with the rate-making principles used during the development of the current Phase I EHF's. The principles also reflect each program's input during the interviews and the web conference calls.

As with any rate-making principles, it should be recognized that, at times, the principles may represent competing objectives. The evaluation/monitoring process should seek to reflect a reasonable balance of all these principles:

1. **The EHF Monitoring/Evaluation Process will help the programs to operate in a fiscally responsible manner and address any operating deficiencies or overages in a timely and responsible way.** The programs are publicly accountable, non-profit organizations that operate in a fiscally responsible manner. To be viable and sustainable, they cannot operate in a deficit position for an extended period of time. Similarly, they cannot collect and retain material surpluses, outside of the OCR and E & E Fund. The EHF Monitoring/Evaluation Process

will assist in identifying operating issues and testing the need for interim EHF adjustments prior to the next full-scale review.

2. **The EHF Monitoring/Evaluation Process will endeavour to ensure fees are set at a level that recovers the cost to deliver the service.** EHF's are set based on an estimate of the amount of materials that will be returned for recycling. As such, at any given time, the over- or under-collection of funds from EHF's is a likely occurrence.
3. **The EHF Monitoring/Evaluation Process will recognize the importance of fee stability.** Stability is important to program members (brand-owners and retailers), the public, and the regulators. Adjustments to EHF's would be considered a last resort in the event of operating deficiencies. The level of the OCR and the timing to the next full-scale EHF review are important considerations in determining whether an interim adjustment to EHF's should be undertaken.
4. **The EHF Monitoring/Evaluation Process will consider the effects of EHF adjustments on cross-subsidization between product categories.** To the extent feasible, indicators should be calculated by Product Fee Category (i.e., desktop computers, laptop computers, display devices, desktop printers and fax machines, and computer peripherals) or by Material Category (i.e., computers, display devices, desktop printer/fax machines/peripherals). This will help to identify the source of the under- or over-collection while also ensuring that if EHF adjustments have to be made, they are being made in a way that respects the need to avoid product cross-subsidization.
5. **The EHF Monitoring/Evaluation Process will be practical and administratively efficient.** The EHF review process should be manageable from a resourcing perspective (i.e., it should not require substantial, additional work) and should fit within the confines of pre-defined blackout periods, advanced notice periods, requirements for Board/government approval, and the preparation of budgets, forecasts, and actual sales and costs. This process is intended to be an internal one.
6. **The EHF Monitoring/Evaluation Process will be done in a manner that is transparent and understandable.** The process, including the approach to revisiting the fees, will be undertaken in a manner that is transparent, replicable, and understandable by the public, brand-owners, regulators, and other relevant stakeholders.

2.2 INDICATORS

As a first step in the review process, different indicators were considered to help identify when program costs and revenues have exceeded a threshold and triggered a review of the EHF's. The Study Team identified and examined several options with the Advisory Committee. Following discussion with the Advisory Committee, two indicators were chosen, both based on variations of a revenue to cost coverage ratio (RCCR). An RCCR of 100% indicates that revenues and costs are equal; an RCCR less than 100% indicates that revenues are less than costs (and therefore that EHF's may be too low); and an RCCR greater than 100% indicates that revenues are greater than costs (and therefore that EHF's may be too high). The following RCCRs are recommended by this study:

1. **Program level RCCR using forecast data.** This indicator is useful for identifying revenue over-collection or under-collection at a program-wide level. This indicator is relatively simple to use, but, in the event of a revenue over- or under-collection, it cannot distinguish between product fee categories, which does not address the issue of cross-subsidization.
2. **Material category level RCCR using forecast data.** This indicator is useful for determining whether there are cross-subsidization issues between specific material categories.² While it is recognized that calculating RCCRs at a product fee category level would provide useful information for interim fee adjustments, it is noted that cost data are not currently tracked or budgeted at the product fee category level.^{3,4}

While an RCCR could be calculated using either actual or forecast data, it was determined through discussions with the Advisory Committee that forecast data was preferred, since it is a forward looking indicator that would improve the ability of the programs to identify and respond to potential problems before they occur.

The entire process is heavily dependent on this initial calculation. It is essential therefore that forecasts be undertaken with the most up-to-date, accurate information that is available, and using sound analytical methods.

2.3 IMPLEMENTATION

Once the indicators were identified, the Study Team proposed a process for reviewing and responding to revenue over-collection and under-collection issues. This proposed process was reviewed with the Advisory Committee during the web conference. Figure 1 outlines the steps involved in the process and further details are provided below. Figure 1 is intended to help guide the decision-making process while allowing a degree of discretion and flexibility.

STEP 1

The first step involves calculating the forecast program level RCCR.⁵ Forecast program level RCCR is calculated by dividing total forecast EHF revenues by total forecast operating and common costs, as follows:

$$\text{Forecast Program Level RCCR} = \frac{\text{Total Forecast EHF Revenues}}{\text{Total Forecast Operating and Common Costs}} \times 100$$

It was noted during the web conference and program interviews that in the event of revenue under-collection, the programs could calculate the forecast program level RCCR taking into consideration cost-cutting measures, such as decreasing funding for certain program activities, as appropriate and feasible.

² 'Material category' for Phase I products refers to one of the following three sets of products: display devices, computers, and printers/fax machines/peripherals.

³ 'Product fee category' refers to a set of designated products to which the same EHF is applied.

⁴ The collection of revenue from EHF's is not connected to the way in which the cost of recycling products is tracked. As such, tracking collection by material category is feasible while tracking by product fee categories is not currently feasible across all programs.

⁵ Although forecast data is preferred for this exercise, it should be checked against actual data to ensure accuracy.

Appendix F provides sample graphics that may help to inform programs on this step. The first graphic is intended to provide a snapshot of a program's RCCR at a specific point in time, while the second provides a better view of the trend over time.

STEP 2

Two results are possible from Step 1:

1. If the forecast program level RCCR is less than 100%, there is a revenue deficiency:

Forecast Program Level RCCR < 100%

- If there is a risk of materially depleting the OCR, then an interim fee adjustment may be required; if there is minimal risk, then an interim fee adjustment may not be required.

2. If the RCCR is greater than 100%, there is a revenue over-collection:

Forecast Program Level RCCR > 100%

- If there is a risk of materially exceeding the OCR, then an interim fee adjustment may be required; if there is minimal risk, then an interim fee adjustment may not be required.

In both cases, the determination of risk would consider the following factors:

- Current level of OCR;
- Timing to next EHF review; and
- Other mitigation options considered by the program Board of Directors.

It should be noted that the level at which the OCR is 'materially' exceeded or depleted will differ between programs. While it may be possible to provide a broad definition of 'materiality', a definition that is too rigid would not allow each program and its Board of Directors the flexibility to consider the unique circumstances of each situation. Therefore, this document does not attempt to provide a definition of 'materiality'.

STEP 3

This step is followed in the event it is determined that an interim fee adjustment is necessary. Step 3 involves calculating a forecast RCCR for each material category (MC) (or, if possible, the product fee category level RCCR). The forecast MC level RCCR is calculated by dividing total forecast EHF revenues from a MC by the total forecast operating and common costs of that MC, as follows:

$$\text{Forecast MC Level RCCR} = \frac{\text{Total Forecast EHF Revenue from MC}}{\text{Total Forecast Operating and Common Costs for MC}} \times 100$$

STEP 4

Step 4 involves determining whether the interim fee adjustment should be different for each material category or a simple equal percentage change across categories. It was noted during discussions with the programs that the equal percentage option would be simpler to implement, but that the programs would

need to consider the implications of cross-subsidization between categories. Therefore, step 4 defines two possible outcomes from the MC level RCCRs calculated in step 3:

1. All MC level RCCRs fall within $\pm 10\%$ of 100%:
 - a. If this is the case, an equal percentage EHF adjustment would be implemented across categories. The program would calculate the percentage increase or decrease in EHF required to achieve a program-wide forecast RCCR of 100%.
2. Some or all MC level RCCRs fall outside $\pm 10\%$ of 100%:
 - a. If this is the case, each MC EHF would be adjusted independently based on its RCCR calculated in Step 3. The program would calculate the percentage change to each of the MC EHFs that would be required to achieve a forecast MC RCCR of 100% for each category. This percentage would be applied to each product fee category EHF associated with the MC.

The approach recommended in this review is consistent with the zone-of-reasonableness (ZOR) concept that was discussed in the 2009 Phase I report.⁶ As with any rate-setting process, it is often not possible to satisfy all rate design principles and criteria simultaneously. The ZOR approach is considered to adopt a reasonable balance between the principle of minimizing cross-subsidization between product categories and the principles related to fee stability, administrative efficiency, and transparency.

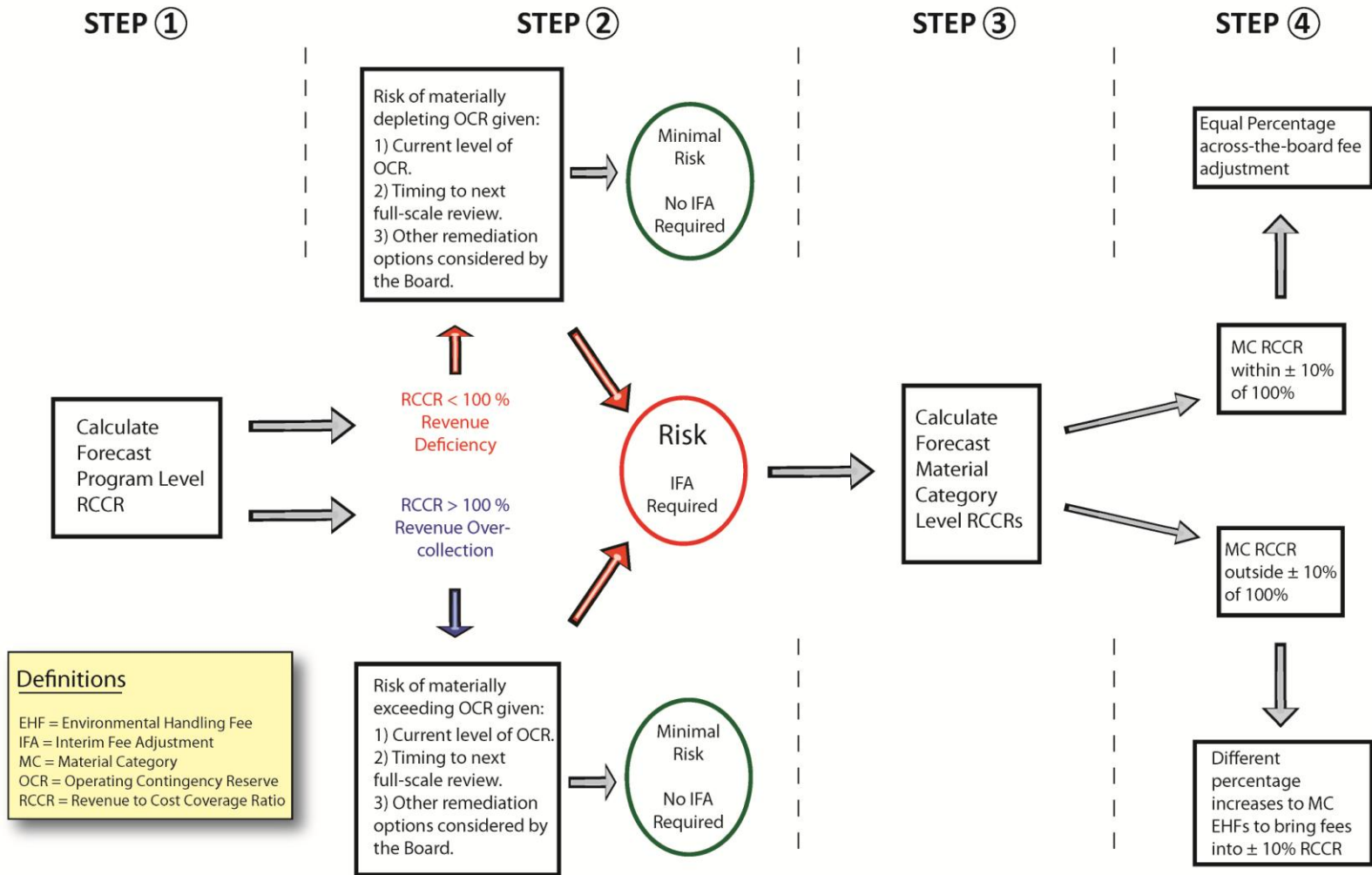
Implementation of this monitoring/evaluation process within the context of regular reporting procedures already in place would be ideal. For example, calculation of a program level RCCR and presentation within regular quarterly (or other) reporting mechanisms to the program management and Board of Directors, would provide a regular opportunity to discuss whether or not action would be required (i.e., moving into Step 2 of the process). This may be preferred over the option of setting specific annual or mid-term timelines.

To the extent feasible, the programs should seek to harmonize their review process timing. In order to facilitate comparisons across jurisdictions, it would be advantageous for the programs to use consistent data collection/sampling methods for collection and processing statistics, as well as consistent accounting and financial reporting of cost information wherever feasible. Progress has been made on harmonization of reporting but continued attention will help ensure meaningful comparisons can be made across jurisdictions.

The process described here has been focused on Phase I where the material and EHF categories are relatively well-defined. Its application to Phase II will likely be a greater challenge (particularly with respect to cost data) due to the larger diversity of material and EHF categories. In this case, greater attention should be given to sampling procedures.

⁶ Phase I Report, p. 45.

Figure 1: EHF Monitoring/Evaluation Framework



3.0 THE OCR AND SPECIAL FUNDS

In addition to the selection of indicators and formulation of a fee review process, the Study Team was asked to consider certain issues related to the Operating Contingency Reserve (OCR) and the Effectiveness and Efficiency (E & E) Fund. Recent directives and actions on the part of the Canada Revenue Agency have indicated that the programs may wish to review the purpose and use of these funds. Appendix B provides a timeline and details related to the development of the OCR.

Interviews were undertaken with program representatives (largely program managers) to gain an understanding of the purpose of these funds from their perspective. With respect to the OCR, these interviews (see Appendix C) indicated three perspectives on the purposes of the OCR:

- To fund a wind-down period (e.g., a sufficient amount of funding to cover a period of time after the program comes to an end, to ensure that products that come in during this period can be recycled);
- To address potential operating risks (e.g., economic downturns, unexpected changes in the rates of return of various electronic products); and
- To handle potential uncertainty associated with the volume and processing costs of discontinued materials (e.g., VCR's).

In the case of the E & E Fund, interview findings suggested that its general purpose was to finance initiatives related to research and development that will improve program performance. Appendix D provides a timeline and details related to the development of the E & E fund.

As the intent of this research was to document current perspectives on the purposes of these funds, not to recommend specific changes, the perspectives noted above may not be complete. Other purposes for both funds may be possible.

It was noted during the program interviews that most programs do not have formal policies setting out the purpose of the OCR and how it is to be used. In contrast, most programs do have policies in place concerning the E & E Fund or the equivalent research and development funds maintained by other programs.

Based on the review undertaken as part of this research, the Study Team recommends that the programs develop (where they do not currently exist) and maintain formal policy with respect to the OCR and E & E funds that specifies the purpose of the fund, the appropriate funding level, and the activities for which it can be used. In both cases (OCR and E & E Fund) the programs may want to achieve a level of consistency (or harmonization) on this issue.

It is recommended that the programs develop formal policies outlining the purpose, use, and appropriate levels for each of the funds. These policies will need to be considered during future EHF reviews.

4.0 SUMMARY OF KEY OUTCOMES AND RECOMMENDATIONS

The purpose of this study was to develop an approach, consistent with program fee-setting principles and methods, that would be used to evaluate the extent to which the revised Phase I EHF contribute to a viable and sustainable program. This approach is also expected to be useful for Phase II.

Following in-depth discussions with the Advisory Committee, the Study Team recommends the programs adopt the following measures outlined in this technical memo:

1. The guiding principles (see Section 2.1);
2. The indicators (see Section 2.2); and
3. The fee review process (see Section 2.3).

These measures are not intended to be overly prescriptive, but rather are intended to provide the programs with a certain degree of flexibility to consider the unique circumstances that may be in place at any one point in time.

The Study Team was also asked to review certain aspects of the OCR and E & E Fund. Based on the review undertaken as part of this research, the Study Team recommends the programs develop (where they do not current exist) and maintain formal policy with respect to the OCR and (E & E Fund policy already in place) that specifies the purpose of the fund, the appropriate funding level, and the activities for which it can be used. In both cases (OCR and E & E Fund) the programs may want to achieve a level of consistency (or harmonization) on this issue.

Finally, a brief communication document was drafted for general use in describing the nature of the current study. This can be found in Appendix B.

APPENDIX A

SUMMARY OF FINDINGS FROM PROGRAM INTERVIEWS

Summary of Findings from Program Interviews

1.0 OVERVIEW

Telephone interviews were conducted with each program in order to gather information and perspectives with respect to the following considerations:

1. How a threshold could be defined to determine whether a fee adjustment is necessary.
2. What actions could or should be taken if a threshold is exceeded.
3. Administrative implications of implementing a fee adjustment.

A brief summary of the findings on each of these topics is provided below.

2.0 DEFINING A THRESHOLD

Options for defining a threshold need to consider the following factors:

1. Actual and forecast program revenues;
2. Actual and forecast program costs; and
3. Availability of data.

In general, the programs indicated a preference for using forecast data to define a threshold, although they saw the utility of using both actual and forecast data. Using forecast data was seen as useful for identifying problems in advance so that steps could be taken to avoid problems, rather than dealing with them as, or after, they happen. Sales and cost updates are prepared on a monthly or quarterly basis among the programs and budgets are prepared annually.

All programs, with the exception of ARMA, noted that program expenditures are tracked on a Material Category basis and not on a Product Fee Category-specific basis.¹ Therefore, it was generally noted that a threshold or indicator would need to take this data limitation into consideration.

There was general agreement that a revenue to cost coverage ratio (RCCR) would be useful in defining thresholds. However, it was noted that calculating RCCRs by Product Fee Category would not be feasible for most programs given the nature of the data collected by the programs (i.e., expenses are not feasible to track by Product Fee Category). On the other hand, calculating RCCRs by Material Category would be feasible for all programs.

3.0 ACTING ON A THRESHOLD

Once a threshold has been surpassed, options for corrective actions must be identified. These options must consider certain mitigating circumstances as well as constraints, including:

1. The level of the OCR and whether it can be used to mitigate revenue shortages; and
2. The timing until the next major review of fees.

Among the programs, there was strong agreement that adjusting EHF's would be the absolute last resort when acting on a threshold. Several programs noted that a temporary fee adjustment without a firm commitment to revisiting the EHF's at a predetermined time would likely create anxiety and uncertainty among program members, the regulator, and the general public. It was noted that cost-cutting measures would be used initially to address any operating deficiencies.

There was general agreement that the decision to implement EHF revisions should consider the current level of the OCR and the timing of the next full-scale EHF review/recalculation. For example, the programs generally noted a preference to avoid a temporary EHF adjustment if the OCR was sufficient to mitigate any revenue shortfalls until a regular, full scale review of the program's EHF's could be undertaken.

It was noted that the OCR is intended to cover six months to two years of operating expenses, depending on the program. The programs raised some concerns regarding recent action on the part of the Canada Revenue Agency with respect to acceptable OCR levels for not-for-profit associations. It was noted during the interviews that to-date none of the programs have had to draw down the OCR to cover revenue shortfalls.

4.0 ADMINISTRATIVE CONSIDERATIONS

During the interviews, the following administrative considerations relevant to the determination of a threshold and implementation of fee adjustments were noted:

¹ The term 'Product Fee Category' refers to the categories of products to which a single EHF has been assigned: i.e., desktop computers, portable computers, display devices, desktop printers and fax machines, and computer peripherals. The term 'Material Category' refers to one of following three product categories: display devices, computers, and desktop printers/fax machines/peripherals.

1. Board approval would be required to implement any threshold indicators and fee adjustment processes. Government approval would be required for ACES and OES. However, any approval process must take into account the total amount of time needed to receive approvals and make changes given other process conditions (e.g., 90-day notice and blackout periods).
2. In the event that changes to EHF are necessary, the programs identified several constraints and requirements that exist to changing EHF. A blackout period for changing EHF essentially exists between August and the end of January. In the case of OES, March is also avoided due to government fiscal year-end spending. Blackout periods may or may not be regulated, but they are closely adhered to. Programs also tend to follow a 90-day lead-in time for EHF adjustments.
3. Each program's Board of Directors would be required to approve EHF adjustments. In some cases, Ministerial approval would also be required following Board approval. It was noted by the programs that in both cases gaining Board or Ministerial approval would likely be more difficult if the recommendation was to increase, rather than decrease, EHF.
4. From an administration perspective, it was suggested that adjusting EHF across material categories, that is, increasing or decreasing all the fees by the same percentage, would be simpler to implement than to adjust each fee individually. However, it was also noted that there would be a need to consider the programs' general preference to avoid cross-subsidization between product fee categories.

APPENDIX B

DEVELOPMENT OF OPERATING CONTINGENCY RESERVE IN USE BY

ACES, ESABC, AND SWEEP

Development of Operating Contingency Reserves in use by ACES, ESABC, and SWEEP

1.0 INTRODUCTION

ACES, SWEEP, and ESABC are not-for-profit, industry-led electronics stewardship programs that are funded exclusively through revenues from environmental handling fees on regulated products. Each of these programs maintains an Operating Contingency Reserve (OCR). At times it has been noted the purpose of the OCR includes:

- To help programs address potential operating risks (e.g., economic downturns that reduce program revenues, unexpected changes in the volume of material returned for recycling); or
- To fund a wind-down period (e.g., a sufficient amount to cover a period of time after the program comes to an end, to ensure that products returned during the wind-down period can be recycled.

Recent directives and actions on the part of the Canada Revenue Agency have prompted the programs to review the current target of a two-year OCR.

1.1 KEY HIGHLIGHTS OF OCR DEVELOPMENT

The following table presents a timeline and key activities related to the adoption of a two-year OCR by ACES, ESABC, and SWEEP:

Timeline	Key Activity	Relevant OCR Details
June 2008	RFP issued to undertake a fee-setting study (focus on Phase II)	EHF-setting criteria outline the need for a one-year OCR.
October 2008	Completion of Phase II Study	Report describes a one-year OCR.
November 2008	Launch of Phase I Study	Same EHF-setting criteria as those outlined in Phase II study (one-year OCR).
December 2008	Study workshop in Vancouver	Option of two-year OCR discussed and noted as the preferred option in order to address uncertainty in program revenues, particularly given the three year period between major EHF reviews.
April 2009	Completion of Phase I Study	Report describes a two-year OCR.

2.0 OPERATING CONTINGENCY RESERVES – TIMELINE OF DEVELOPMENT WITH KEY DECISION POINTS

2.1 PHASE II

In 2008, ACES required a study to analyze and make recommendations for EHF's for "Phase II" regulated products. The initiative was jointly commissioned by ACES, SWEEP, and ESABC and carried out by InterGroup Consultants Ltd. and Forkast Consulting. Guiding principles and criteria that were intended to steer this process were outlined in the project Request for Proposals (June 2008). The third point of the EHF Setting Criteria noted the need for the program (Nova Scotia, specifically) to maintain an operating contingency, per product category, to cover a projected one full year of the operating costs of each category¹.

The resulting fee structure and analysis reflected this one-year OCR. The program EHF-setting criteria were revised to use the following language²:

Criteria #3

Operating Contingency Reserve (OCR): The program will maintain an OCR, per product category, to cover a projected 1 full year of operating costs. This requirement has been included in the development of the common costs used for calculating the EHF's.

¹ Request for Proposal, p. 6.

² Phase II Report, p. 7.

Criteria #4

Accrual of the OCR: The OCR will be accrued until the targeted amount of a projected 1 year of operating costs is achieved. This requirement has been adopted in the development of the cost forecasts to be recovered through the EHF.

2.2 PHASE I

The Phase I fee-setting methodology was initially undertaken using the guiding principles and criteria outlined in the Phase II report (October 31, 2008). However, as the study progressed, the option of a two-year OCR was explored. The decision-making process to get to this point was initiated during the Phase I EHF-setting workshop in Vancouver in December 2008.

Participants from the workshop included:

- Executive Directors for ACES, ESABC and SWEEP;
- Resource Recovery Fund Board (RRFB) – Program manager for ACES;
- Product Care Association (PCA) – Program manager for SWEEP;
- SARCAN Recycling – Collection manager for SWEEP;
- Encorp Pacific (Canada) – Program manager for ESABC;
- Electronics Product Stewardship Canada (EPSC);
- Retail Council of Canada (RCC); and
- Director of Harmonization for ACES, ESABC and SWEEP.

A detailed set of notes for this session was produced³. The topic of operating reserves was first introduced on December 10, 2008 when it was suggested that, according to the preliminary results from InterGroup's analysis, some of the existing EHF's were too high, potentially leading to surpluses (reserves) accruing on a yearly basis. Communication issues associated with the building of these reserves were discussed. One of the participants provided a personal account of a situation in which they were forced to decrease their EHF's to deal with excess reserves and ended up losing all of their reserves when economic conditions changed. An outcome of this initial discussion was that there was good reason to have at least a one-year operating reserve (deemed to be conservative) for Phase I.

This topic was raised again on the following day (December 11, 2008) in discussion related to escalation and the recent economic downturn. Two participants in the workshop raised the possibility of keeping a two-year OCR (rather than a one-year) in order to be cautious. Factors identified as 'reasons to be cautious' included:

- Environment of economic uncertainty;
- Nature of contracts with collectors, processors, etc. (usually fixed, providing limited flexibility in the event of revenue shortfalls)

³ Phase I Vancouver Workshop Meeting Notes.

- Possibility of a number of factors acting in concert to lead to revenue problems (e.g., decreased market for scrap metals, inflationary pressures, and economic downturn in general leading to reduced revenue and increased costs).

The consensus among program personnel at that time was to revisit the EHF-setting criteria to reflect a two-year operating contingency⁴:

Criteria #3

Operating Contingency Reserve (OCR): The program will maintain an OCR, per product category, to cover a minimum projected 2 full years of operating costs. This requirement has been included in the development of the common costs used for calculating the EHF.

Criteria #4

Accrual of the OCR: The OCR will be accrued until the targeted amount of a projected 2 years of operating costs is achieved. This requirement has been adopted in the development of the cost forecasts to be recovered through the EHF.

3.0 CONCLUSIONS AND NEXT STEPS

ACES, ESABC, and SWEEP, have revisited the topic of the OCR on several occasions as part of the review of fee-setting methods. The inclusion of an appropriation to the OCR has been included in program fee-setting guiding principles and criteria.

The transition from a one-year OCR to a two-year OCR was the subject of Phase I fee-setting discussions in Vancouver in December 2008. At that time, the programs were in favour of expanding the OCR from one year of operating expenses to two years of operating expenses, primarily in consideration of the uncertainty created by the economic downturn of 2008.

As part of the mid-term review of the programs' Phase I EHF, it was noted that the programs do not have a formal policy related to the implementation and use of the OCR. It appears the programs could benefit from a more formal policy regarding the purpose and use of the OCR. Allocations to the fund and appropriate uses of the fund will need to be considered during future reviews of the program EHF.

4.0 SOURCES

ACES, ESABC, and SWEEP. *To analyze the Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End-of-Life Electronics Recycling Programs in Canada - Request for Proposal.* (June 2008).

InterGroup Consultants and Forkast Consulting. *Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada - Calculation of Revised Environmental Handling Fees for Phase II Products.* Commissioned by ACES, ESABC and SWEEP (October 31, 2008).

⁴ Phase I Report, p. 7.

InterGroup Consultants and Forkast Consulting. *Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada – Calculation of Revised Environmental Handling Fees for Phase I Products*. Meeting notes from Study Workshop in Vancouver (December 10 and 11, 2008).

InterGroup Consultants and Forkast Consulting. *Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada – Calculation of Revised Environmental Handling Fees for Phase I Products*. Commissioned by ACES, ESABC and SWEEP (April 24, 2009).

APPENDIX C

SUMMARY OF FINDINGS FROM PROGRAM INTERVIEWS: OCR

Summary of Findings from Program Interviews: OCR

1.0 BACKGROUND AND APPROACH

A web conference was held as part of the EHF review study on April 21, 2011. A key outcome of these discussions was the perspective that it would be useful to further investigate the issue of program operating contingency reserves (OCRs). Collectively, it was recognized that there were differences in the way the programs defined, developed, and potentially utilized their OCR.

The intent of this exercise was not to draft a new OCR policy. Rather, the purpose was to document what is currently in place, summarize the perspectives of the programs (including the challenges they encounter in defining the OCR), and identify where there are differences between the organizations.

A series of questions were posed to key program manager personnel that relate to the OCR in use by the respective programs. The purpose of this process was to aid in the establishment of a common definition of the OCR, including how and when it would be used.

2.0 OUTCOMES

2.1 PURPOSE OF THE OCR

- For the most part, there was consistency among the programs regarding at least the initial purpose and development of the OCR. The OCRs have been developed within the context of wind-down costs. It is intended to ensure that, in the event of program termination, sufficient dollars would be available to handle the costs associated with the remaining, incoming materials and administration of that process over a certain period of time ranging from six months to two years.

- Over time, there has been a slight reframing of the perceived purpose of the OCR towards its utility in ensuring some level of stability within the programs, at least for those that do not already have a separate fund that is already set aside for this purpose.
- There is a general view that these two objectives (wind down costs versus funds to tap in the case of revenue shortfalls, for example) need to be addressed separately.
- Challenges identified:
 - Fixed expenditures that extend beyond the timeline of the described 'wind down' period (e.g., office space lease).
 - Level of detail required with respect to expenditure characterization (e.g., different levels of severance pay associated with different employees).
 - Determining the size of the OCR within the context of a wind down scenario is unlikely to reflect the actual volume of materials that would be handled within that time period. The programs are not closely engaged on the product marketing end of the process and will not have a clear idea of exactly what their costs are likely to be throughout this pre-determined wind-down period.
 - Similarly, in the case of program expansion – into other jurisdictions and new product phases – it is exceedingly difficult to determine an appropriate OCR in advance.

2.2 POLICY

- Most programs have some form of documentation outlining the size of the OCR (number of months or years of operating costs). However, most do not have a formal policy describing how it is to be set or used.
- Policy or documentation that is in place would have been Board-approved.
- Overall, there is little policy concerning how the OCR should be developed and used.

2.3 PRODUCT CATEGORY CONSIDERATIONS

- General understanding that there is a need to respect the principle of 'no cross-subsidization'. Some Board members are starting to raise this issue, for example, out of concerns that the OCR collected under Phase I should not be used to address Phase II products.
- Current program policy does not address product fee category considerations but there is an understanding that they will eventually have to.

2.4 WHEN TO USE THE OCR

- There was considerable uncertainty regarding the conditions under which the OCR would be utilized. There was recognition that it could be useful in the case of revenue shortfalls and similar conditions.
- Situations of this kind have not occurred historically. Current policy (formal or otherwise) does not provide clear guidelines.
- It would ultimately be up to the Boards to make the call regarding OCR utilization.

2.5 PROTOCOL/PROCESS

- Use of the OCR would have to be justified and would require Board approval.

APPENDIX D

DEVELOPMENT OF EFFECTIVENESS AND EFFICIENCY FUND IN USE BY

ACES, ESABC, AND SWEEP

Development of the Effectiveness and Efficiency Fund in use by ACES, ESABC, and SWEEP

1.0 INTRODUCTION

ACES, SWEEP, and ESABC are not-for-profit, industry-led electronics stewardship programs that are funded exclusively through revenues from environmental handling fees on regulated products. The Effectiveness & Efficiency (E & E) Fund is intended for research and development initiatives that will improve program performance.

Recent actions on the part of the Canada Revenue Agency suggest that the programs may have to revisit practices concerning the E & E Fund, including the size of the Fund and policy related to its development and utilization.

1.1 KEY HIGHLIGHTS OF E & E FUND DEVELOPMENT

The following table presents a timeline and key activities related to the development of the E&E fund for ACES, ESABC, and SWEEP:

Timeline	Key Activity	Relevant E & E Fund Details
June 2008	RFP issued to undertake a fee-setting study (focus on Phase II)	EHF-setting criteria outline the need for a research and development fund, to be accrued at a maximum rate of 1% of operational costs per product category.
September 2008	Phase II Study workshop in Vancouver	General acceptance of a move from 1% accrual to 5% accrual, recognizing that 1% is not sufficient.

Timeline	Key Activity	Relevant E & E Fund Details
October 2008	Completion of Phase II Study	Report Guiding Principles and Criteria note that funds for research and development projects will be accrued at a minimum rate of 1 per cent and a maximum rate of 10 per cent of operational costs per annum. The language was identical in the subsequent Phase I study.

2.0 E & E FUND – TIMELINE OF DEVELOPMENT WITH KEY DECISION POINTS

2.1 PHASE II

In 2008, ACES required a study to analyze and make recommendations for EHF's for "Phase II" regulated products. The initiative was jointly commissioned by ACES, SWEEP, and ESABC and carried out by InterGroup Consultants Ltd. and Forkast Consulting. Guiding principles and criteria that were intended to steer this process were outlined in the project Request for Proposals (June 2008). The fifth point of the EHF Setting Criteria noted the need for the program (Nova Scotia, specifically) to maintain funds for research and development projects. These funds would be accrued at a maximum rate of 1% of operational costs per product category.

As part of this study, a workshop was held in Winnipeg in September 2008. The following participants attended the workshop:

- Executive Directors for ACES, ESABC, and SWEEP;
- Resource Recovery Fund Board (RRFB) – Program manager for ACES;
- Product Care Association (PCA) – Program manager for SWEEP;
- SARCAN Recycling – Collection manager for SWEEP;
- Encorp Pacific (Canada) – Program manager for ESABC;
- Electronics Product Stewardship Canada (EPSC);
- Retail Council of Canada (RCC); and
- Director of Harmonization for ACES, ESABC, and SWEEP.

During this workshop, consideration was given to increasing the maximum rate of accrual to 5%. As the study drafting entered its final stages the language was revised further, and the fee structure and analysis reflected the same:

Criteria #5

Effectiveness & Efficiency Fund for research and development initiatives: Funds for research and development projects will be accrued at a minimum rate of 1 per cent, and

a maximum rate of 10 per cent of operational costs per annum. This provision will be reviewed in conjunction with the EHF rates. For the purposes of this study, an accrual of 5 per cent of operational costs has been included in the forecast costs assigned to each product category.¹

This language was also used in the Phase I study.

3.0 CONCLUSIONS AND NEXT STEPS

ACES, ESABC, and SWEEP have developed a formal policy related to the development and utilization of their E & E Funds. In the case of OES, potential projects are identified early during budget discussions and the amount of funding required can be estimated and ear-marked for research and development funds.

As with the OCR, allocations to the fund and spending related to the fund will need to be considered during future reviews of the program EHF's.

4.0 SOURCES

ACES, ESABC and SWEEP. *To analyze the Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End-of-Life Electronics Recycling Programs in Canada - Request for Proposal.* (June 2008).

InterGroup Consultants and Forkast Consulting. *Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada - Calculation of Revised Environmental Handling Fees for Phase II Products.* Commissioned by ACES, ESABC and SWEEP (October 31, 2008).

InterGroup Consultants and Forkast Consulting. *Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada – Calculation of Revised Environmental Handling Fees for Phase I Products.* Meeting notes from Study Workshop in Vancouver (December 10 and 11, 2008).

InterGroup Consultants and Forkast Consulting. *Analysis of Environmental Handling Fee Schedules for Selected, Regulated, Industry-led, End of Life Electronics Recycling Programs in Canada – Calculation of Revised Environmental Handling Fees for Phase I Products.* Commissioned by ACES, ESABC and SWEEP (April 24, 2009).

¹ Phase II Report, p. 7.

APPENDIX E
PUBLIC COMMUNICATION DOCUMENT

SUMMARY OF THE REVIEW OF ENVIRONMENTAL HANDLING FEES FOR PHASE I REGULATED ELECTRONICS



INTRODUCTION

Environmental Handling Fees (EHFs) fund the five not-for-profit electronics stewardship programs in Canada. Phase I EHFs, which apply to desktop computers, laptop computers, display devices, printers and fax machines, and computer peripherals, were set by employing a number of assumptions and estimates. Therefore, when these EHFs were set, it was determined that it would be useful to conduct a high-level review of the Phase I EHFs at a pre-determined interval.

InterGroup Consultants Ltd. was retained to accomplish the following objectives:

- Develop an approach that would be used to evaluate the extent to which the revised Phase I EHFs contribute to a viable and sustainable program.
- Determine an indicator (or a set of indicators) that could be used to identify any material problems related to revenue over-collection or under-collection and to ascertain if the EFHs are reasonable.
- Apply the final internal review methodology to test data to determine the accuracy of assumptions/approach and to gauge whether the calculations need to be revised prior to the scheduled three year recalculation of EHFs set for late 2012 or early 2013.

The objectives of this study were accomplished largely through one-on-one discussions with each program's comptroller and conference calls with representatives from each program in attendance.

GUIDING PRINCIPLES

Based on discussions with the stewardship programs, a set of Guiding Principles for Monitoring and Evaluating EHFs was established. These principles were developed to guide the assessment and selection

of monitoring and evaluating indicators. It should be recognized that, at times, the principles may represent competing objectives. The evaluation/monitoring process should seek to reflect a reasonable balance of all these principles:

1. The EHF Monitoring/Evaluation Process will help the programs to operate in a fiscally responsible manner and address any operating deficiencies or overages in a timely and responsible way.
2. The EHF Monitoring/Evaluation Process will endeavour to ensure fees are set at a level that recovers the cost to deliver the service.
3. The EHF Monitoring/Evaluation Process will recognize the importance of fee stability.
4. The EHF Monitoring/Evaluation Process will consider the effects of EHF adjustments on cross-subsidization between product fee categories.
5. The EHF Monitoring/Evaluation Process will be practical and administratively efficient.
6. The EHF Monitoring/Evaluation Process will be done in a manner that is transparent and understandable.

INDICATORS

This study determined that two indicators would be useful in identifying when a threshold to act has been reached. Both indicators use a revenue to cost-coverage ratio (RCCR), which is essentially a ratio of revenue to cost, in conjunction with forecast data.

1. **Program level RCCR using forecast data.** This indicator is useful for determining whether any program-wide issues with EHF's are on the horizon. This indicator is relatively simple to use, but, if it detects an issue, it will not be able to determine which product fee category or categories is/are causing the issue.
2. **Product fee category level RCCR using forecast data.** This indicator is useful for determining whether the revenues of specific product fee categories would be sufficient to cover their costs. However, the data necessary to make this calculation is not currently obtained by most programs at the product fee category level (only ARMA collects this data). It would be possible, however, for all programs to calculate this at the material category level. There are three material categories: computers, display devices, and printers/fax machines/computer peripherals.

IMPLEMENTATION

Based on the guiding principles and the threshold indicators, a framework detailing how a program should act in the event of a material revenue over-collection or under-collection was developed. This framework is not meant to prescribe the exact measures any particular program should take in response to a problem, but it should be of considerable assistance to programs finding themselves in financial difficulties.

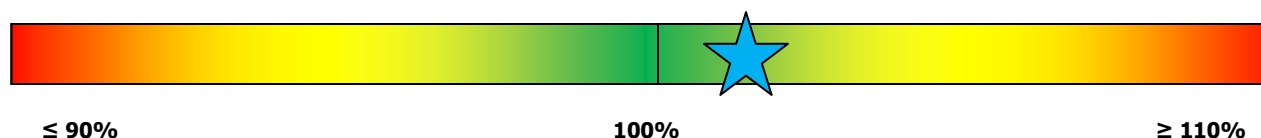
APPENDIX F

SAMPLE DASHBOARD REPORT PRESENTATION GRAPHIC

SAMPLE DASHBOARD PRESENTATION GRAPHIC

Sample Graphic #1:

Period	Type	RCCR
Current Period	Forecast	102%
Previous Period	Forecast	98%
	Actual	94%



Legend

- Green denotes RCCR from 95% to 105%.
- Yellow denotes RCCR from >90% to <95% and >105% to <110%.
- Red denotes RCCR 90% or less and 110% or more.

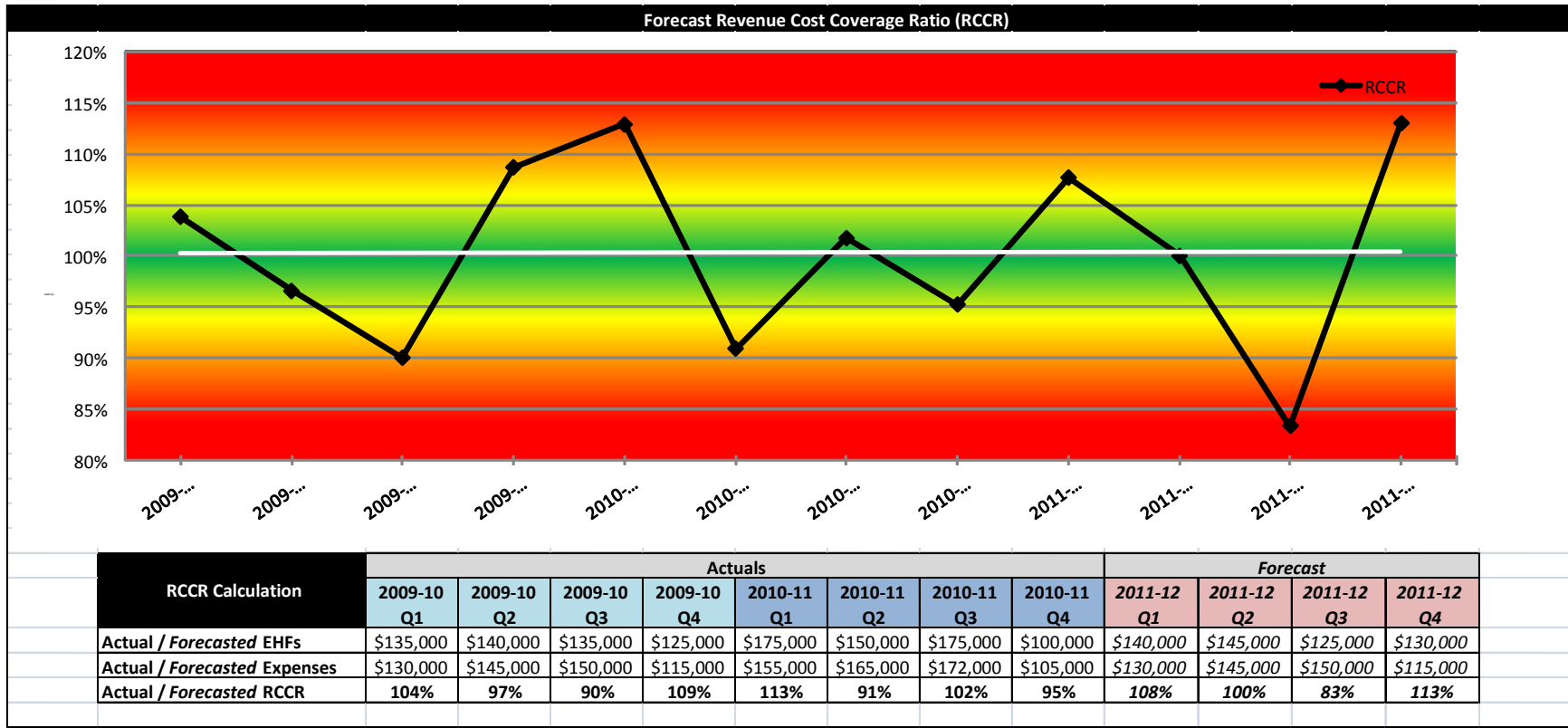
Explanation

Sample Graphic #1 provides a snapshot of the current situation. It can help to anticipate potential issues in the upcoming period (e.g., quarter or year), while also tracking the ability of the program to forecast these issues. In the example above, the current forecast program level RCCR is 102%. This indicates that anticipated revenues exceed the costs required to operate the program.

This compares to the forecast program level RCCR calculated during the previous time frame, which equalled 98% (which indicates that costs slightly exceed revenue according to the forecast).

At the end of the previous time period, when it was possible to calculate an actual RCCR, it was found that the ratio was 94%, which is a more serious concern than was anticipated by way of the forecast.

Sample Graphic #2:



Legend

- Green denotes RCCR from 95% to 105%.
- Yellow denotes RCCR from >90% to <95% and >105% to <110%.
- Red denotes RCCR 90% or less and 110% or more.

Explanation:

This graphic could be used as additional support in decision-making processes. Unlike Sample #1, this would illustrate quarterly trends for past (actual) RCCR's in addition to the upcoming, forecast RCCR's. It also provides a sense of potential volatility. In addition, for ease of calculation, the values for revenues and costs can be directly input into the table. The trend line running through the graphic will help the programs to monitor overall progress.