



## PRELIMINARY ANALYSIS

May, 2011

### Visibility of Eco-Fees in Producer Responsibility

#### Executive Summary

Allocation of responsibility and the funding of agreed approaches are fundamental tenets of producer responsibility. These two key issues are inextricably intertwined and both are ultimately affected by whether eco-fees for program funding are 'visible' to consumers or 'hidden' in product prices for producer responsibility programs.

A recent article in the Canadian Tax Journal and a critique of the article debated whether visible or hidden eco-fees best met the objectives of extended producer responsibility. The Global Product Stewardship Council examined these articles as part of ongoing efforts to understand and implement producer responsibility initiatives to better internalise product life-cycle costs with product prices and provide incentives for producers to reduce the environmental impacts of their products.

Most producer responsibility legislation is mute on whether fees should be visible or hidden, and neither the article nor the critique provides compelling arguments to dictate fee visibility either way. It is understood that there is a growing political debate in Canada whether or not to be more prescriptive on fee visibility, so this polarising issue is likely to become even more prominent. Greater understanding of the circumstances under which each approach works best is necessary to better inform any such political decisions, but either approach is doomed without meaningful stakeholder engagement and consumer education.

As various jurisdictions around the world face budget deficits and debate the role of producer responsibility in addressing these deficits, funding and allocation of responsibility will continue to be intertwined and debated. Further research and debate is needed on the ultimate impact of eco-fees (whether visible or hidden) on consumer and producer behaviour. One additional concern is whether the number and variability of producer responsibility initiatives risks diminished returns over time given competition for consumer attention and interest. Integrated collection systems may help address such concerns but further complicate debate over fee visibility.

#### Introduction

Traditionally, extended producer responsibility (EPR) was applied to items that are toxic, hazardous or difficult to manage. By requiring producers to internalise the costs of managing these products at end of life (EOL), EPR would in theory lead to product re-design to minimise environmental harm and shift EOL management costs from local waste management programs to producers. Product stewardship was generally regarded as a voluntary approach to EPR, while in Canada the terms became interchangeable. Over time, components of each approach have merged into an approach we'll call 'producer responsibility' for simplicity's sake. Allocation of responsibility and the funding of agreed approaches are fundamental tenets of producer responsibility. These two key issues are inextricably intertwined and both can ultimately be affected by whether eco-fees for program funding are 'visible' to consumers

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or ‘hidden’ in product prices for producer responsibility programs (visible fees do not arise in shared responsibility programs).

In Canada, as in the US, Australia and other countries, solid waste management and recycling are the responsibility of provincial/state and local governments. Approximately 65 producer responsibility schemes have been legislated in Canada over the past decade. Under most of these programs, industry pays the full costs of EOL management of their products but has flexibility in program funding and implementation.

In an article for the Canadian Tax Journal<sup>1</sup>, Canadian consultant Duncan Bury posits that eco-fee-included (‘hidden’) pricing provides incentives for improving products’ environmental performance and shifting responsibility to producers, as well as achieving other EPR objectives. A critique of the Bury article<sup>2</sup> by Neil Hastie and Malcolm Harvey countered that the benefits of eco-fee-excluded (‘visible’) pricing justify its use in “*all but the most unusual of political circumstances*”. Hastie and Harvey contend that visible fees are preferred for brand owner compliance, cost accountability for consumers and result in higher profiles for producer responsibility programs.

Both the article and critique were prompted by retraction in late 2010 of phase 2 and phase 3 of Ontario’s Municipal Hazardous and Special Wastes (MHSW) EPR program following consumer outcry and political backlash. Phase 2 products included batteries, pharmaceuticals, sharps, fluorescent light bulbs and mercury-containing products. Phase 3 materials included flammables, toxics and corrosives.

After a three month review period and temporary funding through Ontario’s environment ministry, the ministry cancelled phases 2 and 3 of the MHSW program. As a result of the program’s retraction, producers were not held responsible for phase 2 and phase 3 products - phase 2 costs were allocated to the provincial taxpayer and phase 3 costs were allocated to local/municipal taxpayers.

Debates about fee visibility span such diverse elements as fiscal responsibility and tax policy, producer responsibility, consumer awareness and education, supply chain competition and responses and the ultimate impact of eco-fees on consumer and producer behaviour. This analysis is intended to help frame the debate on the circumstances under which each approach works best and raise issues that warrant further research.

## **Analysis**

It should be stated from the outset that it is difficult to point to clear examples of EPR and cost internalisation having direct impacts on its two fundamental intended outcomes: 1) product re-design to minimise environmental harm and 2) shifting EOL management costs from local waste management programs to producers. Contributing factors to each of these outcomes (as elaborated by Hastie and Harvey) are so varied that direct cause-and-effect relationships are difficult to discern. Unfortunately, perceptions and political reality (remember in politics, ‘perception is reality’) all too often become principal measures of success in judging whether producers have been held accountable to an appropriate level of responsibility.

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<sup>1</sup> Duncan R.W. Bury, *Policy Forum: Should Extended Producer Responsibility Programs Use Eco-Fee-Included Pricing?* Canadian Tax Journal (2010) vol. 58, no. 4, 927-50, available at [http://www.ctf.ca/ctfweb/EN/Publications/CTJ\\_Content/2010CTJ4.aspx](http://www.ctf.ca/ctfweb/EN/Publications/CTJ_Content/2010CTJ4.aspx), accessed January 2011.

<sup>2</sup> *Eco Fees-Hidden or Visible?* undated, by Neil Hastie (President and CEO, Encorp Pacific (Canada)) and Malcolm Harvey (Principal, M E Harvey and Associates), available at [http://www.globalpsc.net/downloads/Hastie\\_Harvey\\_Bury\\_Eco-Fees\\_Critique\\_0211.pdf](http://www.globalpsc.net/downloads/Hastie_Harvey_Bury_Eco-Fees_Critique_0211.pdf).

### Ontario's Phase 2 and Phase 3 MHSW Fee Experience

Bury<sup>3</sup> suggests that the failure of Ontario's phase 2 MHSW fee implementation (phase 3 materials were not specifically addressed, although were likely included by Bury under phase 2 materials) "*points to the need for governments to look more closely at the EPR eco-fee-included pricing mechanism and at the programs in New Brunswick and Quebec, and to be more prescriptive regarding cost internalization by producers*". Facts in evidence do not bear out this assertion. As Hastie and Harvey note<sup>4</sup>, British Columbia "*has had stewardship programs with visible eco fees for a wide range of consumer products and packaging since the mid 1990's with little controversy*".

A common belief about Ontario's experience with phase 2 and phase 3 materials was that the fee's failure can be attributed to an uncharacteristic lack of stakeholder engagement and consumer education by Stewardship Ontario. However, Stewardship Ontario spent over \$2.5 million in radio, TV and outdoor advertising during the first week of the launch alone – more than any other producer responsibility program in Canada at that time. In addition, Stewardship Ontario sent eco-fee communication packages to over 3,500 retailers in the province. These figures have since been eclipsed by the Ontario electronics program, but they were still significant. Indications are that most of the advertising was intended to guide consumers on where to return products, rather than to explain the fee changes, which may have had some impact on the debate. Ontario's experience with implementing producer responsibility programs should have also minimised conflicts.

Perhaps other issues were responsible that were not addressed by either the Bury article or the Hastie and Harvey critique. The fact that a provincial election was being held within one year from program introduction was certainly a contributing factor to the debate.

In addition, Ontario's phase 2 products are increasingly common in producer responsibility programs and reasonably straight-forward to define and track. However, phase 3 materials, which included an estimated 6,500-10,000 product SKUs, were by far the most problematic as they were everyday consumer products that in most cases required little or no EOL management if the consumer "consumed" the entire product. Polling by Stewardship Ontario showed a consumer perception that these materials ended up attracting an eco-fee to subsidise the wasteful habits of a minority of consumers and the eco-fees were therefore unfair. These perceptions were compounded by some incorrect fee calculations by retailers passed on as visible eco-fees and an aggressive anti-fee media campaign.

As a result of the programs' retraction, producers were not held responsible for phase 2 and phase 3 products in Ontario - phase 2 costs were allocated to the provincial taxpayer and phase 3 costs were allocated to local/municipal taxpayers. This result runs counter to the intended objectives of producer responsibility, so it is worth considering other hypotheses. It is possible that Ontario's phase 3 expansion, in particular, overshot consumer willingness to see product stewardship visibly applied and reflected in a visible eco-fee for each discrete item and that this over-reach coincided with increased 'anti-tax' sentiments that fuelled the debate. A greater proportion of hidden eco-fees on these items may have avoided some of the criticism. Most brand owners did not pass on the Stewardship Ontario fees for these materials to their retail customers. Some retailers added fees simply on the basis of the Stewardship Ontario published charges to producers.

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<sup>3</sup> Bury 2010, p.927

<sup>4</sup> p.2

The GPSC analysis of Ontario's experience has a more nuanced view of fee visibility than either the Bury article or the Hastie and Harvey critique. It does not make sense to apply a given eco-fee approach, whether visible or hidden, to all programs regardless of the product type. Rather, it may be that visible eco-fees are best applied to products that have higher concerns about toxicity, are relatively expensive and/or are consumed over a relatively long period of time, while hidden eco-fees are best applied to less potentially toxic, more common items with higher turnover. Preferred eco-fee approaches are also likely to emerge under given circumstances given varying levels of public concern, stakeholder engagement and supply chain interests, so prescriptive approaches may prove counterproductive. Innovation on funding mechanisms will likely prove more necessary than ever as the scope of producer responsibility initiatives expands and as debate over their application becomes more intense.

A related issue that warrants further examination is whether there is a point of diminishing returns in applying producer responsibility to such a broad range of products that objective analysis, consumer concern, consumer/ratepayer interest and political reality simply cannot support such application. It is difficult enough to identify the full cost impacts of a given product or material type and to encourage consumer returns of items that are already covered under producer responsibility programs without delving into the huge grey area of products with marginal or debatable impacts. It is important to note here that the basis for the Stewardship Ontario fees was actually reported costs being incurred by municipal programs. One contributing error was the refusal to allow a de minimis provision for the relative tiny proportion of material returned vs. consumed in use.

Clear, meaningful selection criteria are likely to become more critical to ensuring ongoing program support and involvement. Integrated collection systems spanning a range of products or material types may become more cost effective means of ensuring returns, however their funding could become even more problematic.

Bury contends that Ontario's phase 2 MHSW controversy shows governments can no longer avoid the eco-fee visibility issue by defaulting to producer responsibility organisations (PROs) that prefer visible fees. As a result, Bury suggests that governments are likely to become more prescriptive about eco-fees in the future. Hastie and Harvey view this political response as an indication that governments do not trust the PROs' ability or commitment to stakeholder awareness. Regardless, Canadian governments in particular may feel increasingly compelled to take stands on eco-fee visibility. An important aspect to be addressed is whether governments are willing to state that it is the producer's responsibility to fund the program as they saw fit and that consumers could refuse to pay the fee or buy the product.

### **Consumer and Supply Chain Awareness**

Bury states, *"Calling the fee an "environmental handling fee," or an "eco fee," or an "environmental disposal fee," to name a few examples, tells the consumer very little. What informs the consumer is a proper, widely visible and available communications and advertising program explaining why the fee exists and how it will be spent. This kind of communication and a comprehensive plan to roll it out is what is necessary and should not be confused with the supposed communication of the added price itself."* This communication should also not be confused with fee visibility. Visible eco-fees are not necessary to communicate to the public that the cost they are paying for the product includes EOL environmental management, although a range of manufacturers prefer visible fees for precisely this reason.

Experience suggests that while consumer awareness and education are instrumental to gaining program acceptance, supply chain awareness and response may be far more instrumental to achieving program objectives.

In the early 1990's, Florida implemented a market-based advance disposal fee (ADF) of one or two cents per container on designated cans, bottles, jars and beverage containers. Exemptions were made available for achieving material recycling rates, using specified levels of recycled content or recycling an equivalent amount of material from the waste stream in Florida.

Due to the level of government involvement, the Florida ADF would not be considered an example of producer responsibility. It does, however, demonstrate the importance of supply chain pressures. Retailers weakened consumer notification provisions contained in original proposals; as a result, consumers generally knew little about the fee. However, the supply chain did know about the fee and means of gaining exemption. Demonstrated improvements in recycling activity resulted from the supply chain not wanting products to be associated with the fee, even though the fee was only one or two cents per container.

In the European Union, white goods manufacturers traditionally supported visible fees, especially since product take-back costs were relatively high and visible fees were seen as a means of increasing consumer awareness. Moreover, the take-back measures often started out in a voluntary, sector-wide and collaborative spirit. Gradually, these visible fees became institutionalised, there was no need to reduce them and retailers in some countries got to keep a substantial share of the fees to cover administrative costs. In addition, there was an agreed period of transition under the Waste Electrical and Electronic Equipment (WEEE) Directive to account for the need to flush out orphan and historical wastes.

Information and communication technology (ICT) producers in the EU, on the other hand, began rejecting visible fees early on (except in Belgium). The fee amounts for ICT equipment are relatively small, there is a huge variety of products (which bloats administrative costs), and distribution chains are complex. For this sector then, hidden fees seemed a more appropriate fit.

Greater understanding is needed on the impacts of eco-fees on consumer decisions. For hidden fees, do consumers understand that the fees are incorporated in the product price and the reasons for their imposition? The same goes for visible fees. Even where fees are visible at check-out, to what extent does the fee affect consumer purchasing, especially when compared to traditional factors such as price, quality and brand loyalty?

### **Tax and Ratepayer Implications**

In theory, eco-fees (whether visible or hidden) would be seen by consumers as user fees rather than as taxes and seen as a means of reducing general costs of local government waste management costs. The eco-fees considered here are charged by PROs to cover their costs for discharging producer responsibility requirements. As Bury notes, these eco-fees are determined by and remitted to the PRO and are therefore not taxes. Rather, they are more of a fee-for-service.

The reality, however, is that consumers tend to see the eco-fees as taxes unless they have a reasonable understanding of the rationale for the fee. This perception is unfortunately reinforced by the fact that there are no prominent examples of rate reductions to taxpayers as a direct result of product stewardship or EPR program implementation. Rather, further increases are not necessarily required in local taxes to fund rising waste management and recycling costs or these costs do not require diversion from other municipal services such as schools or fire protection. The objective of transferring cost from the ratepayer to the consumer goes back to the program commonly cited as the first example of EPR – the 1991 German Packaging Ordinance. Ratepayer costs might not go up as much as they otherwise might have, but we are not aware of any examples where rates specifically went down as a result of producer responsibility program implementation.

Recycling collection, and to a lesser extent waste collection, is a labour-intensive operation that gets more expensive every year, while demands and legal requirements for higher and higher standards of waste management mean that infrastructure has to be constantly improved.

Although Germany touted reduced waste management costs as a reason for the introduction of EPR, these costs did not go down as supporters of EPR expected for a variety of reasons:

- stricter legal requirements on landfilling and large investments in alternative methods of treatment/disposal;
- diverting roughly 20% of household waste into the Dual System made little difference to the vehicle movements needed to collect the remaining waste; and
- rising wage costs for a very labour-intensive activity (see above).

Unfortunately, many local governments are still not aware of the full costs of managing specific products and pricing of recycling and waste management services is not precise enough to pass along cost savings from managing specific products through producer responsibility.

Even though PROs are often not-for-profit corporations (some private companies have entered the market in Germany, Poland, the UK and elsewhere) and do not receive government funds, it could be argued that the public has a right to know how PROs spend the fees they collect. Consumers are ultimately responsible for both the eco-fees and for paying rates, so it is important to be able to understand how funds are being spent either way. While most consumers might not take the time to investigate, transparent, verified information should be available for those that do care enough to investigate (audited financial statements are required to be made public in British Columbia). This objective can be achieved regardless of whether the eco-fees are visible or hidden.

### **‘Design for Environment’ Implications**

The potential for product re-design to minimise environmental harm (“design for environment” or DfE) through EPR varies by products: there has been little so far for WEEE, but EPR has had some DfE impact on packaging. Procurement costs, transport costs (minimising vehicle movements), technological ability to meet functional requirements and consumer demand all have a greater effect on packaging design than weight-based fees, especially since international companies mostly use the same packaging across countries and the ratio of fees for different materials can vary greatly from country to country (particularly in Europe). Fees probably have a greater impact on design in the case of companies operating solely or mostly in high-fee countries like Germany and Belgium, but even there consumer expectations for packaging choices will be more influential than fees.

The biggest packaging weight reductions took place in the 1970s and 1980s, when technology allowed major lightweighting initiatives to take place, and also allowed plastics to substitute for heavier materials for carbonated drinks and other products. For most WEEE in Europe, there was little if any separate collection of the affected products and their environmentally sound management before EPR legislation was introduced. Therefore, municipalities had no associated costs which a shift of responsibility to producers could lower. However, a variety of municipalities in Europe and elsewhere were becoming increasingly mindful of the potential cost impacts to provide environmentally sound management of a much broader range of products.

## **Impacts on harmonisation**

Perhaps Bury's most compelling argument on hidden fees relates to harmonisation<sup>5</sup>:

*“It might also be the case that eco-fee-included pricing would be valuable in helping to promote more harmonized programs. The issue of different fees in different jurisdictions is a challenge to manage in areas where populations share an interprovincial boundary, such as Ottawa and Gatineau, or Lloydminster, or in cases where there is easy access to the market of an adjoining province. Consumer purchases may be influenced if an alternative purchasing location with a lower fee is easily available. Differing fees also lead to higher administrative and management costs for producers that have to remit fees to PROs in different jurisdictions that use different fee-costing models. Visibility only exacerbates the issue. If the eco fee is included in the price, the producer will have more flexibility to harmonize prices between adjoining jurisdictions.”*

Hastie and Harvey state that one of the benefits to visible fees is that *“changes in fees don't require changes to retail and wholesale price lists or advertisements”*. This is a key payoff for brandowners where harmonising by using visible fees can minimise disruptions in their pricing schemes.

Potential for harmonisation represents one of the most significant opportunities to improve the quality of and reduce the costs of producer responsibility schemes. But if national companies are compelled to pay fees (in particular if they are hidden) at a province or state level, they will spread these costs over all products sold nationally even though consumers in the other jurisdictions are not receiving PRO services.

Would this lead to more producers willing to 'hide' the fee if they can avoid cross-border issues? If so, could visibility address some issues such as EU distortions in data resulting from cross-border issues? Once a program is truly national (as in many EU countries) producers are more willing to internalise costs, particularly as they do not affect national pricing policies).

## **Conclusions**

The GPSC Executive Committee made a conscious decision to stay mute on the issue of the visibility of fees, as have the regulators and designers of many producer responsibility programs. The GPSC's Product Stewardship Principles and Actions state *“all product lifecycle costs – from using resources, to reducing health and environmental impacts throughout the production process, to managing products at the end-of-life – should be included with the total product cost”*. Furthermore, some leading practitioners define EPR programs as internalising EOL management costs to the producers *and consumers* of the designated products rather than the local tax base.

Neither the Bury article nor the Hastie and Harvey critique provides a compelling argument to mandate that fees be either visible or hidden; this can be attributed in part to strong views on both sides of the debate, but also to a significant lack of available, objective data on the impacts of eco-fee visibility on consumer behaviour. Both articles do, however, underscore the polarity of this issue and the range of economic and political considerations that must be taken into account and are therefore helpful contributors to the debate.

PROs charged with funding product stewardship and EPR programs are held accountable to producers that are ultimately held accountable by consumers. There is a collective interest in discharging

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<sup>5</sup> Bury, p.943

obligations at minimal cost and avoiding consumer backlash. As long as externalities associated with a given product are ultimately included with the product cost to consumers, why should governments introduce unnecessary difficulty and risk political turmoil, when such decisions can be left to producers, retailers and PROs under a performance-based approach?

Until now, most governments have been reluctant to take a position either way, although there is anecdotal evidence that governments (Canadian governments in particular) may feel increasingly compelled to take stands on eco-fee visibility. Given the potential economic and political repercussions, there is a clearly demonstrated need for a greater understanding of the circumstances under which each approach works best.

Given the polarity of eco-fee visibility, these issues are best examined in an independent, objective manner with evidence-based examples and meaningful stakeholder engagement. Further research and debate is also needed on the ultimate impact of eco-fees (whether visible or hidden) on consumer and producer behaviour.

This analysis was prepared by Russ Martin, President of the Global Product Stewardship Council. In the early 1990's, Russ was responsible for development and implementation of Florida's market-based Advance Disposal Fee on cans, bottles, jars and beverage containers.

Primary documents include:

- Duncan R.W. Bury, *Policy Forum: Should Extended Producer Responsibility Programs Use Eco-Fee-Included Pricing?* Canadian Tax Journal (2010) vol. 58, no. 4, 927-50.
- *Eco Fees-Hidden or Visible?* undated, by Neil Hastie (President and CEO, Encorp Pacific (Canada)) and Malcolm Harvey (Principal, M E Harvey and Associates).

Duncan Bury Consulting, Encorp Pacific (Canada) and Stewardship Ontario are all members of the Global Product Stewardship Council. Duncan Bury is a former Environment Canada official responsible for monitoring Canada's EPR programs.

Neil Hastie currently serves on the GPSC Executive Committee.

This analysis was reviewed by the GPSC Executive Committee and various anonymous reviewers prior to release.