



31 May 2013

Position Paper on Waste Management Policy

1. Executive Summary

Waste management in Latvia is an industry with a significant potential for development and investment. The sectoral policy has a direct effect on the competitiveness of companies.

The situation in the waste management sector allows us to identify a number of structural issues in the business environment. It is insecure and unfavourable to investment:

- **Competition restrictions** – unreasonable restrictions of competition in an industry where the market has a sufficient number of interested players and a proven positive effect of free market on the price and quality of services;
- **Lack of transparency** – a business environment that is not transparent to the players involved or potentially interested and to the public at large;
- **Monopolisation** – The waste management market is being gradually monopolised by the municipalities on weak economic grounds or on political grounds alone; the entrepreneurs are losing their market share and scope for recouping their investments in the industry.

When carrying out its statutory duties the municipality should ensure that its actions help to protect and represent the interests of municipal residents and entrepreneurs alike, and to use its funds efficiently. FICIL believes this can be achieved as follows:

- Create a system that enables each municipal resident to receive necessary services at the best possible price;
- Ensure that the legal and practical solution to providing the service chosen by the municipality helps to put into practice the strategy documents it has adopted on social and environmental issues; and
- Refrain from engagement, or assess the need to engage, in business where competing services rendered by private entities are readily available in the market segment, thus providing and enhancing healthy competition.

Municipal decisions and actions in organising household waste management should serve as a tool for ensuring that the objectives set in the national and EU policy documents are achieved and government tasks performed.

Government agencies currently lack effective policies, which should be put in place to ensure that the waste management business in Latvia operates as a single system. An insufficient and poorly organised flow of information makes it impossible to properly evaluate the contribution of services rendered by entities owned by private and public bodies to achieving the objectives defined in Latvia's environmental policies and international commitments

1. Recommendations

1. Comprehensive waste management policy, adequate control and supervision, involvement of all interested parties, and process transparency

- (a) Create an institutional model that ensures the implementation of comprehensive waste management policy: consistency of the national/regional environmental policy objectives, adequate control and supervision, and involvement of all interested parties. Purposefully ensure that the process and information are transparent.
- (b) Build cooperation between municipalities and private service providers based on civil mechanisms by properly separating political and commercial responsibility for achieving the policy objectives at local or regional level.
- (c) Prepare quantitative long-term objectives for the treatment and economically sound use of the buried waste. Assess the effectiveness of applicable rates of natural resource tax (NRT) in connection with the environmental policy objectives for restricting waste burial.
- (d) Assess the performance of the packaging management system in terms of effectiveness.

2. Free and fair competition towards effective work and good result

- (a) Encourage free and fair competition in the waste management market by removing legal and political obstacles to the participation of companies in the waste management market, including obstacles created by any municipal activities inconsistent with good governance.
- (b) Enhance competition in the business segments by legally strengthening the separation of waste material management/treatment activity from waste burial.
- (c) Separate the policy objectives for managing waste created by households and waste resulting from business.

3. Economically sound, restricted business of public persons, and control over it

- (a) Develop legal restraints to municipal business activity that is not objectively based on essential public interests; ensure effective control over the operation of this system that helps to achieve the objective by municipal companies competing on an equal footing with private market players.
- (b) Build a system for the constant and adequate (based on the situational analysis and oriented towards achieving the objective) implementation and supervision of control over these restrictions.

2. Rationale for our recommendations

1. Create an institutional model that ensures the implementation of comprehensive policy, adequate control and supervision, involvement of all interested parties, and process transparency

The current legislation and policy documents fail to provide for a clear notional or institutional link between the autonomous functions (and objectives) of each municipality in organising waste management services in its area and achievement of the objectives set in the environmental law and policy documents, for example, a reduction in the amount of waste buried in landfills.

The waste management procedure set up by the Natural Resource Tax Act, which is intended as an administrative tool for encouraging the implementation of environmental policy, after a change in the actual market situation and policy objectives, currently distorts competition by deepening

the deficiencies and ineffectiveness of policy, including unreasonable municipal engagement in business, and hinders achievement of the national environmental policy objectives.

There are no effective, motivating mechanisms for deterring breaches or for a meaningful penalty in the event of a breach.

1.1. Interaction between waste management policy and environmental policy: policy making, implementation, and supervision

The functions and tasks of the Ministry for Environmental Protection and Regional Development (VARAM) as the agency in charge of this field require it to —

- draw up, organise and coordinate policy on environmental protection and regional development;
- oversee the legitimacy of municipal operations and the performance of tasks set for the municipalities;
- draw up action plans to reduce pollution; and
- supervise the legality of municipal activity.ⁱ

The current legislation merely declares VARAM's functions and tasks; the ministry has not been granted decision-making rights for performing these functions. So there is no functioning mechanism for supervising and controlling municipal activities.

There are no legally binding duties or objectives of the municipality as the service organiser within the national policy, including municipal responsibility for their implementation by organising local waste management services. None of the parties ensures the collection and transparency of shared and complete information about the activities of the waste management system to its members (see Appendix 1).

Precisely defining and separating the responsibility areas of the parties involved in the provision of services, and using the most appropriate legal form for carrying out their duties and tasks, may bring economic and public benefits.

1.2. Management system capable of operating without subsidies includes “internal” support mechanisms. Effective use of NRT for achieving policy objectives.

The objective of NRT is to promote the efficient use of natural resources, to restrict environmental pollution, to scale down the production and sales of environmentally polluting goods, to encourage the introduction of new, environmentally friendly technologies, to support sustainable development of the economy, and to provide funding for environmental protection efforts.

The current arrangements for allocating NRT revenues in circumstances of restricted competition encourage actions that aggravate the problems identified above, rather than addressing them, and thus threaten not only the creation of a sustainable waste management solution but, from a broader perspective, the implementation of environmental policy.

The situation where municipal companies manage all national household waste landfills, while at the same time receiving 60% of the NRT paid on environmental pollution, including on waste burial in their area,ⁱⁱ fails to promote the municipal interest in reducing the amount of buried waste and encouraging waste treatment (objectives included in the national policy documents). There is no mechanism for verifying or monitoring the link between the NRT paid and the amount of waste actually managed.

NRT rates are an effective tool for stimulating the reuse, treatment and recovery of waste, and thus a reduction in waste volume. A change of tax policy, especially in the short term, may serve as a welcomed boost and catalyst for change.

Cancelling the allocation of NRT on environmental pollution to the special municipal budget for environmental protection in the part that is calculated for waste burial, would remove the municipal interest in increasing the amount of waste buried in landfills. The municipalities would be motivated to promote the development of waste treatment/recovery business in their areas and thus reduce environmental pollution and develop new business.

1.3. Motivation of the state, municipalities and private persons in implementing policy objectives

To eliminate the conflict of interest embedded in the existing municipal system, which distorts competition and hinders the implementation of the overall policy, the waste material management / treatment activities should be legally separated from waste burial.

The liability of waste makers and waste management service providers for failure to comply with waste management requirements should be defined, including with respect to separate collection of waste.

Moreover, the NRT charge setting procedure based on the principle that the waste maker must pay for the amount of waste actually made, would serve as a motivating factor for creating a waste management system oriented towards the achievement of national policy objectives.

Currently neither public information nor the system of information flow within the industry helps to verify the extent to which the tax paid has indeed achieved the objective (see paragraph 2.1 above).

2. Ensure free and fair competition in the waste management market for more efficient achievement of policy objectives

The waste management policy created by the state, including its objectives and costs, is determined by the objective interests of society and Latvia's international commitments on environmental issues. Competition and free market help to achieve these objectives—

- in a better and more efficient way,
- without placing an extra burden on the municipal and national budgets,
- by reducing the cost to the resident without using cross-subsidies, and
- by giving companies a proper choice to determine their costs and therefore competitiveness.

Over two-thirds of the Latvian municipalities, which created close to 80% of the total volume of waste in Latvia in 2012, had restrictions on free and fair competition in their waste management service market without reasonable legal and economic grounds (see Appendix 2).

2.1. Efficiency

A procurement competition helps to choose and, by using the mechanisms specified in the contract, to directly influence the quality of services received and their conformity to the objectives and criteria.

It is in the company's interests to carry out the exercises entrusted to it as efficiently as possible by ensuring the implementation of the task set by the municipality and achieving more accurately the target through the economical and waste-free use of resources.

At the same time, it is possible to develop entrepreneurial investment and to boost capacity by using internal resources, including the expertise of foreign partners, and without making any additional new investments. A saving reduces the cost of service.

2.2. Reduced burden on municipal and national budgets

Assuming that one resident on average makes 1.85 cu.m of household waste a year, it follows that in the regions where a procurement competition was held, one resident on average pays Ls9.29 for household waste removal a year.

In the regions where a procurement competition was not held, one resident on average pays Ls16.39 for household waste removal a year, or where waste is removed by a municipal company, one resident on average pays Ls16.30 for household waste removal a year.

It follows that residents and entrepreneurs of the regions where a procurement competition was not held in 2012 overpaid about **Ls 10,623,326** for waste removal a year (see Appendix 3).

However, even if the residents overpay, most of the municipal waste management companies make no profit or operate at a loss.

2.3. Lower cost to customers without cross-subsidies

Practice suggests that the parish municipalities are currently using cross-subsidies to "regulate" the price to individual customers. Retaining these cross-subsidies is a significant argument for keeping the existing policy that restricts competition and the entrepreneur's freedom of action. At the same time, even if operating ineffectively, the waste management companies established by municipalities receive national/municipal subsidies and apply for EU funding.

Evaluation of the draft Cabinet Regulation on criteria for a household waste maker that is exempt from paying NRTⁱⁱⁱ and permitted to contract with a household waste management entity of his choice shows that a key risk in the opinion of the interested parties is the inability, after losing the amount of waste to be managed, to ensure the existing cost of service to other customers of the service provider chosen by the municipality:

"It is possible that some of the exempt companies will refrain from concluding or terminate their contracts with waste managers chosen by the municipality, and will themselves choose a waste manager. This might reduce the volume of household waste managed by the waste manager chosen by the municipality. This may cause the residents of a particular administrative area to see an increase in the waste management charge. This increase will be associated with the volume of household waste to be collected and its percentage in the particular area."^{iv}

This argumentation is clearly contrary to the "polluter pays" principle established by Directive 2008/98/EC on waste. Moreover, in a free service market situation the companies competing in the market segment would certainly determine and control this process (pricing).

2.4. Right of companies to decide their cost items, ensuring competitiveness

A municipality's decisions regarding the waste industry directly affect each resident as well as the companies operating in its area. Waste management costs may represent a significant portion of expenditure for companies producing goods and services alike.

The inability to influence this cost category may become a significant obstacle to a company's competitiveness or decision regarding investment in an administrative area.

3. Restrict central and local government business that is not objectively based on essential public interests to create a truly free service market

The Administrative Division of the Latvian Supreme Court has found^v that the business of public persons is permissible only in exceptional cases where there is special justification for the conduct of such business, because the objective of public persons is not to make a profit, and the engagement of these persons in business poses a market distortion risk.

Thus, Latvian legislation implies the municipal duty to carry on business only in special, exceptional circumstances.

The European Court of Justice (ECJ) has made it clear that cooperation between government agencies cannot call into question the main objective of the Community rules for public procurement, namely the freedom of provision of services and unhindered competition in all member states,^{vi} while any exception to the procurement procedure must be interpreted narrowly. The burden of proof in such cases lies with the person invoking an exception to the procurement procedure.^{vii}

The grant of waste management rights to municipal companies without applying the public procurement procedure in Latvia is based on the Public Procurement Act, section 3(1)(7). However, its provisions arise from the ECJ case-law findings about instances where it is considered that a procurement contract has not been concluded, and only for the sake of more transparent and easier application of the law, this is included in the above-mentioned clause providing for exemptions from the application of the law.

Given that the activity of municipal entities leads to restricted competition and has practically created a monopoly position for the municipal entity in a sufficiently substantial part of the internal market, the actions of municipalities, without holding procurement competitions for awarding waste management rights, are contrary to the freedom of services and fair competition rules enshrined in EU law and ECJ case law.

FICIL believes that central and local government business should arise from a necessity that is supported by economic and social reasons. In all other cases the municipality should choose a service provider in a competition subject to the public procurement procedure.

The legislation for the public service should clearly separate certain market segments, thereby ensuring better defined market conditions and more efficient use of municipal resources as the municipalities engage in business (doing only the necessary).

Municipal engagement in business is permissible and reasonable only if the market fails to offer an appropriate service. The legislation governing the activities of central and local government should specify instances where a municipality—

- is permitted to engage in business and establish a municipal company for conducting this business;
- should provide that the primary criterion for municipal engagement in business is the

market's inability to provide the particular service;

- should prove compliance with the relevant criteria that allow the municipality to engage in business by preparing and submitting to VARAM for approval a detailed rationale, including a business plan, business principles, and the funding model;
- is required to terminate business and transfer the provision of services to private companies.

Institutionally united or departmental supervision should be set up (following the common guidelines) because it helps to identify strategic tasks or objective deficiencies in the market requiring state intervention and to monitor the future usefulness of this decision.

For example, VARAM's charter should specify the task of not only supervising but also controlling the legality of municipal engagement in business. This would result in VARAM being authorised to take decisions about the usefulness of municipal business and might really influence and ensure the implementation of the environmental protection and regional development policy.

Appendices

Appendix 1. *Policy implementation controls*

The situation in the waste management industry cannot be substantially changed without substantially changing the understanding of tasks of the parties for ensuring a good result.

- The state is already responsible for drawing up an environmental policy, yet we should strengthen the supervision of institutions in charge and control over its fulfilment. By assuming responsibility for implementing the environmental policy in its area, the municipality should ensure that objectives and result indicators are in place by inserting them expertly and conscientiously in the procurement specifications for household waste management. The objectives and result indicators to be inserted in the procurement specifications should be prepared according to the guidelines set at ministerial level.
- When undertaking civil commitments towards the municipality as a result of procurement, entrepreneurs should implement the environmental policy objectives and bear responsibility for the result. The liability (penalties) should be set in the contract between the municipality and the entrepreneur.
- To honour their contract, companies must supply the National Environment Service, which is subordinated to VARAM, with complete information about waste flows, which would help to aggregate this data and assess the achievement of national as well as municipal objectives. Waste flow details are being presented already, yet their accuracy is doubtful because data corruption may be due to the fact that waste is managed by entities formed by municipalities, as their engagement means pursuing diametrically opposite interests.
- It is necessary to provide publicly available information about activities within the waste management cycle.

Appendix 2. *Economic benefits in circumstances of free competition*

Viesīte parish in Zemgale is one of the least populated parishes in Latvia. Waste is managed by a company in which the municipality holds shares. The charge for household waste removal is Ls19.67/cu.m. In a similar region where a procurement competition was held, for example, in Dundaga parish, the waste management charge is Ls3.91/cu.m, which is Ls15.76 less.

One resident on average makes 1.85 cu.m of household waste a year. Thus, one resident of Viesīte parish pays Ls36.39 for waste removal a year, which represents 38% of the national family benefit for one child a month.

Comparing all 22 parishes where an open competition for waste management was held, the service charge to a person was on average 33% less than in other parishes of Latvia (not taking into account Riga where structure of the waste management market significantly differs in the rest of the country) or by 43% when considering the data about the city of Riga.

The regions where a procurement competition for waste management should be held (excluding Riga) have an average rate of Ls 8.81/cu.m. The regions where waste is managed by a company in which the municipality holds shares have an average rate of Ls 8.79/cu.m. The regions where the procurement procedure was applied have an average rate of Ls5.02/cu.m, a reduction of 43%.

Appendix 3. Calculation of overpayment

Procurement competitions for waste management are not held in 97 of the 119 Latvian parishes. In some of these municipalities the waste management service is provided by municipal companies, meaning that these municipalities are undertaking in-house procurement. In another considerable segment of these municipalities a procurement competition is not held at all because the legislation lacks mechanisms capable of influencing municipal omissions in complying with public procurement rules, and so the municipalities are not interested in taking any steps to change their present waste managers.

The present situation in waste management and its adverse effect on the price of the waste management service are illustrated by the following figures (see table 1).

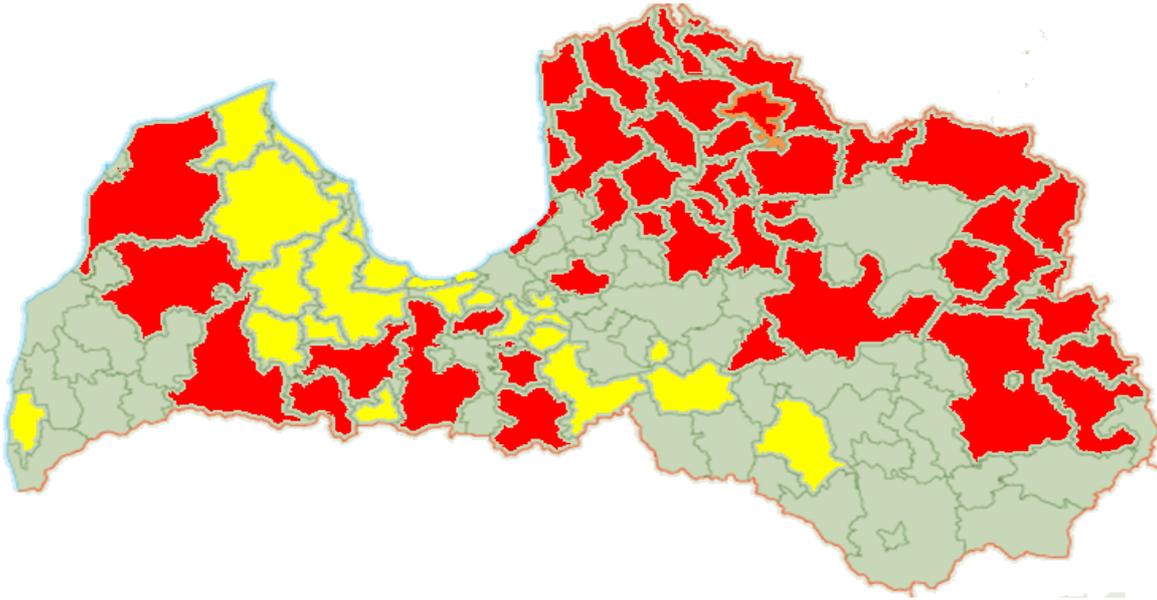
Table 1

Parishes/ towns (type)	Count	Average price Ls/m3	1 person creates waste/m3 a year	Population	Parish/town population's overpayment a year	1 resident's overpayment a year (Ls)	Overpayme nt in region	Overpayment %
Competitions held	22	5.02	1.85	266,821	2,477,967	9.29	-	0%
Waste managed by municipal company	54	8.79	1.85	626,066	10,180,772	16.26	4,174,117	41%
Where competition should be held	42	8.81	1.85	518,884	8,457,031	16.30	3,467,383	41%
Riga (competition should be held)	1	4.90	1.85	658,640	5,970,572	9.07	-119,411	-2%
TOTAL	119			2,070,411	27,086,341		7,522,088	
Overpayment %							28%	
Total Latvian waste market					38,162,193			
Including traders*					11,075,851			
Overpaid by traders*							3,101,238	
TOTAL OVERPAYMENT IN LATVIA							10,623,326	
Overpayment %							28%	

- Data on the commercial (traders) segment of the market is an assumption, based on the segment of the market in Riga, extrapolating to regions and the whole of the territory of Latvia, while considering objective factors such as intensity of commercial activity in the region.

Residents annually overpay a total of **Ls 7,522,088** for waste management in the parishes where waste is managed by municipal companies or where procurement competitions should be held. When including the overpay of entrepreneurs the overpay reaches as much as **Ls 10 326 326**.

Illustration 1



Data: FICIL/private waste management companies
Source: Public information made available by central and local government agencies

ⁱ VARAM charter, part II

ⁱⁱ Natural Resource Tax Act, section 28(2)

ⁱⁱⁱ Draft Cabinet Regulation on criteria for a household waste maker that is exempt from paying NRT and permitted to contract with a household waste management entity of his choice": <http://mk.gov.lv/lv/mk/tap/?pid=40240799&mode=mk&date=2013-01-15>

^{iv} Draft Cabinet Regulation on criteria for a household waste maker that is exempt from paying NRT and permitted to contract with a household waste management entity of his choice": <http://mk.gov.lv/lv/mk/tap/?pid=40240799&mode=mk&date=2013-01-15>

^v Ruling of 29 March 2010 on case SKA-340/2010

^{vi} See ECJ ruling of 9 June 2009 on case C-480/06, paragraph 47

^{vii} See ECJ ruling of 11 January 2005 on case C-26/03, paragraph 46; ruling of 13 October 2005 on case C-458/03, paragraph 63; and ruling of 11 May 2006 on case C-340/04, paragraphs 55 and 58