



California Used Mattress Recovery and Recycling 2019 Program Budget

July 1, 2018

Updated July 9, 2018

Submitted by:

Mattress Recycling Council California, LLC
501 Wythe Street
Alexandria, VA 22314-1917

Submitted to:

California Department of Resources Recycling and Recovery
Scott Smithline
Director
1001 I Street
Sacramento, CA 95812-4025



July 1, 2018

Scott Smithline
Director
California Department of Resources Recycling and Recovery (CalRecycle)
1001 I Street
Sacramento, CA 95812-4025

Dear Director Smithline:

The Mattress Recycling Council California, LLC (MRC) is a tax-exempt non-profit entity certified by CalRecycle as a "mattress recycling organization." MRC was established for the express purpose of designing, implementing and administering mattress recycling programs for California and other states that have enacted mattress recycling laws.

Pursuant to Section 42988 of the California Public Resources Code, MRC hereby submits its proposed 2019 budget.

Please contact me should you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read "Ryan Trainer".

Ryan Trainer
President
Mattress Recycling Council California, LLC

California Used Mattress Recovery and Recycling Plan Budget

Pursuant Cal. Pub. Res. Code § 42988 and 14 CCR §18963, the Mattress Recycling Council California, LLC (MRC), a non-profit corporation, is pleased to submit to the California Department of Resources Recycling and Recovery (CalRecycle) its 2019 budget.

1. Introduction

In September 2013, California enacted SB 254, codified beginning at Section 42985 of the California Public Resources Code, which requires mattress producers to create a statewide recycling program (the Program) to collect and recycle mattresses and foundations discarded in the state. The Program is funded by a visible recycling charge collected from consumers and other purchasers on the sale of each mattress and foundation for use in the state. Pursuant to Cal. Pub. Res. Code § 42987, CalRecycle has certified MRC as the mattress recycling organization to administer the Program.

As required by Cal. Pub. Res. Code § 42987(a)(3)(B), MRC consulted with the mattress recycling advisory committee several times in 2018, prior to the submission of the 2019 budget (and the 2017 annual report).

In terms of the content of this budget, Cal. Pub. Res. Code § 42988 provides that it must meet the following requirements:

On or before July 1, 2015, and on or before July 1 annually thereafter, the mattress recycling organization shall prepare and submit to the department a proposed used mattress recycling program budget for the following calendar year that includes all of the following:

- a) Anticipated revenues and costs of implementing the program, including related programs, projects, contracts, and administrative expenses.
- b) A recommended funding level sufficient to cover the plan's budgeted costs and to operate the mattress recycling program over a multiyear period in a prudent and responsible manner.
- c) The amount of the mattress recycling charge and itemization of costs that each charge covers.

In addition, CalRecycle has issued 14 CCR §18963(b), which provides as follows:

- b) In addition to the requirements of subdivisions (a), (b), and (c) of section 42988 of the Public Resources Code, the information submitted in the used mattress recycling program budget shall contain the following:

- 1) Contact information. Identify the corporate officer of the mattress recycling organization responsible for annual used mattress program budget submittal.
- 2) Anticipated revenues and costs. Describe anticipated revenues and costs of implementing the program, including related programs, projects, contracts, and administrative expenses.
- 3) Mattress recycling charge and itemization. Identify the amount of the mattress recycling charge, including an itemization of costs that each charge covers.

Pursuant to these provisions, MRC has calculated a “recommended funding level sufficient to cover the plan’s budgeted costs and to operate the mattress recycling program over a multiyear period in a prudent and responsible manner.”

In preparing this budget, MRC has allocated revenues and expenses in accordance with Generally Accepted Accounting Principles, as requested by 14 CCR §18962(a)(6).

2. Executive Summary

Based on MRC’s actual expenses and revenues, projected expenses and revenues through 2018, and this proposed 2019 budget, MRC proposes to maintain a \$10.50 charge per mattress or foundation unit sold in California in 2019.

3. Anticipated revenues and costs of implementing the program, including related programs, projects, contracts, and administrative expenses

(Cal. Pub. Res. Code § 42988(a))

In preparing this budget, MRC calculated its revenues and costs as follows:

Revenue

Other than a modest amount of interest income earned on reserves, the recycling charge collected on all sales of mattresses and foundations (collectively referred to as “Units”) is the Program’s only source of revenue. MRC is budgeting Program revenue of \$43,982,799 for 2019.

In preparing the Program’s 2019 budgeted revenue, MRC considered its 2017 actuals and its 2018 first quarter actuals, then estimated (based on the International Sleep Products Association’s (ISPA) Industry Forecast (ISPA Forecast) for 2019 units sold) whether 2019 Program revenue will increase from that level.

The most recent ISPA Forecast anticipates that 2018 units sold will be 1.5%

higher than 2017, and that units sold in 2019 will increase an additional 2%. Therefore, MRC has budgeted 2019 revenue based on a 2% increase in units over 2018 projections, multiplied by a recycling charge of \$10.50/unit.

In 2017, actual Program revenue was 4% below the initial 2017 budget submitted in 2015. Through the first quarter of 2018, actual Program revenue was less than 1% lower than YTD 2018 budgeted revenue. Since Program revenue is directly related to unit sales, this means that 2017 full year and 2018 first quarter unit sales in California were very close to the quantity of units that MRC had anticipated would be sold during those periods, giving us confidence in the methodology used to develop the 2019 revenue budget.

Costs

For purposes of preparing this budget, MRC has classified its expenses under the following categories:

- Collection
- Transportation & Recycling
- Communications/Education and Outreach
- Research
- Administration
- CalRecycle Oversight

Following is a description of each of the above cost categories:

Collection:

This cost category covers the following activities:

- Solid waste facility handling fees
- Consumer incentive payments
- Collection/storage container rental fees and signage
- Illegally Dumped Mattress Collection Initiative

Transportation & Recycling:

Transportation

MRC uses third parties to transport mattresses from collection sites to recyclers for processing. Transport costs vary considerably depending on the transport distance, geographic location of the collection site and container used to hold discarded mattresses.

As the U.S. and California economies improve, inflation and transportation costs are increasing significantly. MRC has budgeted 2019 transportation costs based on (1) 2018 first quarter actual per unit freight rates, plus general inflation and an amount to cover potential fuel cost increases through 2019, multiplied by (2)

the number of units we expect to transport in 2019. To this amount, we have also added a contingency factor in case the Program incurs unforeseen added transportation costs as the Program expands in 2019.

All transportation services are provided by third parties. No MRC staff are directly involved in transporting discarded mattresses. As a result, no direct staff expenses are charged directly to these activities.

Recycling

MRC-contracted recyclers' costs are increasing as labor markets tighten and raise wages, energy costs rise, and other operational expenses are affected by inflation. In addition, the limited secondary markets for recycled materials, reduces the opportunities for recyclers to off-set recycling costs by selling these goods at reasonable prices. Therefore, MRC's 2019 budget for mattress recycling expenses anticipates an increase in per unit processing costs over 2018 YTD actuals. Budgeted recycling expenses also are higher because MRC expects that the Program will increase the number of mattresses recycled by 9% in 2019. Finally, the 2019 recycling budget includes additional expenses that the Program might incur in the event that one or more contingencies occurs.

All recycling services are provided by third parties. No MRC staff are directly involved in processing discarded mattresses. As a result, no direct staff expenses are charged directly to these activities.

Communications/Education and Outreach:

MRC's comprehensive communication and consumer education and outreach efforts inform the industry and consumers about the Program and how to recycle mattresses in California. MRC advertises the Program across the state during key mattress sale weekends. In 2019, MRC plans to increase its advertising frequency and target larger media markets including Los Angeles and Oakland/San Francisco.

Throughout the year, MRC also uses public service announcements, social media and online advertising to communicate with consumers. In addition, it allocates advertising funds to smaller local or regional campaigns that promote new collection sites and events. MRC expects to increase the number of collection events in 2018 and 2019, reaching portions of the state that are not yet serviced by a permanent collection site. In addition to consumer outreach, MRC will continue to communicate with mattress retailers and other members of the industry regarding their legal obligations to register, report, and remit the recycling charge, as well

as how they can recycle the discarded mattresses that they collect from consumers with the Program.

The California marketing and communication expenses cover the following activities:

- Advertising and Consumer Education
- 3rd Party PR Agency
- Industry and Stakeholder Outreach
- Community Collection Events/Conferences and Events
- Other Marketing and Communications Expenses
- MRC marketing and communication staff

Research:

MRC seeks to improve the sustainability of mattress recycling through efforts focused on advancing the efficient collection, transport and recycling of discarded mattresses and identifying new and better uses for extracted mattress components. MRC supports applied research and development efforts intended to achieve one or more of the following objectives:

- Reduce costs and improve the efficiencies of collecting, transporting and recycling discarded mattresses
- Identify and promote mattress recycling best practices
- Foster innovation, cooperation and communication between suppliers, manufacturers, dismantlers and end-market commodity buyers
- Identify new or better uses for recycled mattress materials

Planned MRC 2019 research expenses which support the goals outlined above are as follows:

- In early 2018, MRC participated in events and meetings with similar organizations around the globe to investigate and explore best practices and new markets research initiatives. These activities are extremely helpful in comparing experiences and sharing successful practices. MRC plans to continue these activities in 2019 and the future.
- Now that the Program is fully launched in California, MRC plans to improve the efficiency of our operations. Given that it is expensive to transport light and bulky products like discarded mattresses over long distances, MRC plans to study the transport aspects of its collection network. It will task consultants with identifying steps MRC can take to be more efficient in purchasing and allocating freight resources around the state.
- MRC initiated a project in 2018 to compare the costs and efficiencies of manual and mechanized dismantling and sorting

processes used to recycle discarded mattresses. MRC plans to complete the initial phase of this study in 2019, and may at that time decide to expand it to include other aspects of the mattress collection and dismantling process.

- In the third quarter of 2018, MRC plans to hire a consultant to initiate a research program to identify new markets and uses for post-consumer materials, thereby increasing the recyclability of used mattress materials. This program will continue in 2019 and beyond.
- In 2018 and 2019, MRC plans to conduct a study that will examine whether communities that offer no-cost bulky item curbside collection service have lower incidences of illegal mattress dumping. This study will involve the use of data that MRC has collected from participants in its illegally dumped mattress initiative and a survey of solid waste collection programs across California.
- MRC currently compensates its contracted recyclers on the number of units they deconstruct. MRC will study the pros and cons of shifting to a weight-based compensation process.

MRC has included funds in its 2019 budget for these purposes.

Administration:

This category reflects MRC's expense to administer the Program. This cost category covers the following:

- Management and Staffing
- Travel/field visits
- Legal fees
- Government Affairs
- Annual Financial Audit and Tax Filing Preparation
- Compliance and Service fees
- Bank Fees

Management and staffing includes the salaries and associated overheads of MRC staff that administer the Program. Travel/field visits covers travel costs for staff to visit solid waste sites, recyclers, other operational service providers, and other business-related travel.

Legal costs cover fees for outside counsel that negotiate MRC contracts, address contract compliance issues and advise MRC regarding corporate matters. Government affairs activities include communicating with members of the California legislature and executive branch agencies regarding MRC's plans and accomplishments, addressing their concerns, participating in recycling and related policy discussions, and providing input on specific legislative proposals.

MRC's financial records are audited annually by an independent certified public accountant. MRC also incurs costs in preparing and filing necessary tax documents. Separately, MRC uses both in-house and outsourced providers to confirm whether vendors providing mattress processing services to MRC are complying with their contractual and other legal obligations. The 2019 budget reflects MRC staff and third-party costs associated with conducting these activities.

CalRecycle Oversight:

Cal. Pub. Res. Code § 42988.2 requires that MRC reimburse CalRecycle for its direct costs incurred to implement and enforce the Act. The expense identified on this line item reflects MRC's estimate of these reimbursements for 2019.

4. A recommended funding level sufficient to cover the plan's budgeted costs and to operate the mattress recycling program over a multiyear period in a prudent and responsible manner
(Cal. Pub. Res. Code § 42988(b))

Cal. Pub. Res. Code § 42988 requires that MRC maintain a reserve that is sufficient to fund the Program's operations over a multiyear period in a fiscally prudent and responsible manner. The amount that MRC sets aside in this reserve is influenced by several factors.

First, the Program must be able to adjust to unforeseen circumstances that can have a substantial impact on MRC's expenses. These circumstances could include accidents and disasters; operational and financial failures of MRC's systems, retailers and other sellers that collect the charges, etc. Significant or sudden changes in market dynamics that affect costs (e.g., fuel) or failure of secondary markets for recycled components, political uncertainties,¹ or any combination of the above could also significantly affect the Program and its budget.

Second, the reserve helps protect the long-term viability of the Program by setting aside money that can fund unusual short-term budget deficits without needing to resort to temporary increases in the recycling charge collected on new mattress sales. For example, MRC is budgeting a net deficit for 2019 that includes, among other things, unusual expenses that the Program might incur in the event that one or more significant one-time contingencies occurs. This budget deficit will be funded by the reserve.

¹ For example, a global trade war could have dire consequences for U.S. recyclers that rely on foreign markets for their materials. Likewise, the ballot in this year's California state election will include a proposition that, if approved, could initiate a process to divide California into three separate states. Such an outcome could pose innumerable and costly operational and financial challenges for the Program.

Third, MRC's ability to operate prudently over a multi-year period depends in part on MRC's forecasted operating and administrative expenses for several years into the future. For the next several years, MRC expects to increase its expenditures as it develops the Program's collection network, broadens its geographic coverage, and increases the number of units collected and recycled. This growth will result in MRC's annual budget getting larger in 2020 and the future.

Finally, MRC must be prepared in case its revenue stream (that is, recycling charges collected on the sale of mattresses) is significantly and suddenly disrupted. This could include a downturn in the U.S. economy (which hurts mattress sales) or other events that are external to the Program itself, like legislative or regulatory initiatives that disrupt sales. For example, the California legislature is considering a bill this year (Assembly Bill 2998) that would prohibit the use of flame retardants in mattresses and other products. Under federal law, all mattresses sold in the United States must meet federal flammability standards. Those rules functionally necessitate the use of some flame retardants. The version of the bill that passed the Assembly earlier this year would have created an irreconcilable conflict between a mattress manufacturer's ability to meet the federal standards and comply with California law. Had that version been enacted into law, no mattresses could be sold in California after January 1, 2020, thereby eliminating MRC's funding source. The bill is now pending in the Senate, where it has been amended to narrow, but not eliminate, its impact on future mattress sales. If the bill is eventually enacted, it will hopefully include this important amendment, but that is not a certainty. More importantly, this legislation illustrates how MRC's revenue source is vulnerable to changes in state laws and regulatory policies.

For these reasons, MRC has budgeted to build a reasonable financial reserve equal to twelve months of annual operational expenses that it anticipates it will incur over the next several years. Based on the objectives discussed above regarding MRC's budgeted operational expenses and reserve needs, MRC proposes a total charge-related funding level of \$43,982,799 in 2019 (that is, revenues generated exclusively from recycling charges, and excluding interest and other gains on MRC's reserves) to meet the requirements of Cal. Pub. Res. Code § 42988(b).

5. The amount of the mattress recycling charge and itemization of costs that each charge covers

(Cal. Pub. Res. Code § 42988(c))

Determination of Two Separate Charges

Cal. Pub. Res. Code § 42989(b)(2) gives MRC the discretion to either (1) set a single recycling charge that applies to all sizes and types of mattresses and foundations, or (2) set up to two different charges "to accommodate mattress size differentials." MRC considered whether to exercise its authority to set two

charges when it submitted its Plan in 2015, but decided to set a single charge for all sizes and types of mattresses and foundations. Likewise, MRC has set a single state-specific recycling charge for mattresses and foundations sold in the other two states in which it administers similar mattress recycling programs: Connecticut and Rhode Island.

When CalRecycle approved MRC's 2017 budget, the agency requested that MRC consider two separate charges when it prepared its 2018 budget and discuss this issue with the advisory committee. Pursuant to CalRecycle's request, MRC discussed this topic with the Advisory Committee in June 2017, and explained the rationale for retaining the single charge for calendar year 2018. Likewise, MRC has decided in preparing its 2019 budget to continue to set a single charge, as it is authorized to do by Section 42989.

Itemization of the Mattress Recycling Charge

Cal. Pub. Res. Code § 42988(c) and 14 CCR §18963(b)(3) requires that MRC itemize the costs that the charge covers.

The per unit charge can be distributed over the different cost components discussed above that comprise MRC's 2019 budgeted expenses as follows:

Cost Category	Percent of Per Unit Charge Itemized to Each Category
Collection	12.2%
Transportation & Recycling	66.0%
Communication/Education and Outreach	9.5%
Research	2.1%
Administration	8.6%
California Oversight	1.6%
Total	100.0%

Amount of the 2019 Charge

MRC has gained valuable experience from its first two and a half years of operations in California regarding how best to structure the Program for continued growth, improved efficiency, and effective consumer outreach. The 2019 budget anticipates that the volume of units on which the charge will be collected will increase by 82,134, that the number of units processed through the Program will increase by 129,000 units, and that Program expenses in 2019 will increase by \$7.7 million. Therefore, we conclude that the current charge of \$10.50 is sufficient to fund 2019 expenses while maintaining a reasonable reserve.

6. Contact information. Identify the corporate officer of the mattress recycling organization responsible for annual used mattress program budget submittal (14 CCR §18963(b)(1))

The MRC Budget is submitted by:

Catherine Lyons
Manager
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Alexandria, VA 22314
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7. Anticipated revenues and costs. Describe anticipated revenues and costs of implementing the program, including related programs, projects, contracts, and administrative expenses

(14 CCR §18963(b)(2))

See Part 3 above.

8. Mattress recycling charge and itemization. Identify the amount of the mattress recycling charge, including an itemization of costs that each charge covers

(14 CCR §18963(b)(3))

See Part 5 above.

9. For used mattress recycling program budgets submitted on or by July 1, 2017 all actual expenses incurred to date shall be included. For annual reports submitted thereafter, the previous two years of actual expenses shall be included (14 CCR §18963(b)(4))

Expense Categories	2016	2017	Total
Operations	\$ 12,117,303	\$ 20,294,173	\$ 32,411,476
Cal-Recycle Oversight	\$ 1,853,965	\$ 447,048	\$ 2,301,013
Legal	\$ 84,567	\$ 89,488	\$ 174,055
Marketing	\$ 1,394,990	\$ 1,902,326	\$ 3,297,316
Administration & Research	\$ 1,919,878	\$ 2,564,379	\$ 4,484,257
Total	\$ 17,370,703	\$ 25,297,414	\$ 42,668,117

**Mattress Recycling Council California LLC
2019 Budget**

	2019 Budget	Expense Allocation
REVENUE:		
Fee Revenue (\$10.50/unit)	\$ 43,982,799	
Interest & Dividend Income	\$ 295,800	
Total Revenue	\$ 44,278,599	
 EXPENSES:		
Collection, Recycling, Transportation Costs		
Collection	\$ 4,369,683	
Containers	\$ 1,046,052	
Transportation	\$ 5,549,377	
Recycling	\$ 23,859,969	
Total Recycling, Transportation, and Operational Costs	\$ 34,825,081	78.2%
 Administration & Legal		
Management and Staffing Expenses	\$ 2,787,061	
Travel / Field Visits	\$ 80,386	
Legal	\$ 175,000	
Government Affairs	\$ 300,000	
Annual Financial Audit and Tax Filing Preparation	\$ 100,578	
Compliance and Service Fees	\$ 272,825	
Bank Fees	\$ 122,771	
Total Administration & Legal	\$ 3,838,621	8.6%
 Cal Recycle Oversight		
State Regulatory Oversight Fees	\$ 705,550	
Total Cal Recycle Oversight Fees	\$ 705,550	1.6%
 Communications/Education & Outreach Costs		
Advertising and Consumer Education	\$ 2,535,494	
3rd Party PR Agency	\$ 535,370	
Industry and Stakeholder Outreach	\$ 99,677	
Community Collection Events/Conferences & Events	\$ 688,894	
Other Marketing & Communications Expenses	\$ 100,015	
MRC Marketing & Communications Staff	\$ 262,465	
Total Education & Outreach Costs	\$ 4,221,915	9.5%

Research & Development Costs		
Research & Development	\$ 949,500	
Total Research & Development Costs	<u>\$ 949,500</u>	2.1%
Total Expenses	<u>\$ 44,540,667</u>	100.0%
Operating Net Assets	<u>\$ (262,068)</u>	