CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Les White

SUBJECT: RECYCLE PLUS-- SUPPLEMENTAL 2 OF 4

DATE: August 16, 2006

SUBJECT: RECYCLE PLUS—SUPPLEMENTAL #2, "MACIAS RESPONSE TO CWS COMMENTS AND RESPONSE TO MACIAS REPORT"

REASON FOR SUPPLEMENTAL

On August 10, 2006, the Administration forwarded to the City Council a report entitled "Final Report-Recycle Plus RFP Procurement Process Review" issued by Macias Consulting Group. On August 11, 2006, during the Recycle Plus Study Session, the City Council asked Macias to respond to CWS' correspondence (Attachment A). Attached, please find Macias' supplemental report (Attachment B). In addition, included are the Department of Finance's findings of a recent Compliance Review (Attachment C) and determinations.

Why is tracking solid waste important for the City?

Municipal Code Chapter 9.10, Solid Waste Management, outlines the City's requirements "necessary for the promotion, protection and preservation of the health, safety and general welfare of the people of the city of San José." There are two main reasons why the City is obligated to and interested in tracking the collection of solid waste: (1) financial and (2) regulatory compliance.

Through the Department of Finance, the City regularly conducts compliance reviews pertaining to the payment of Solid Waste Enforcement Fees (SWEF). There is a financial obligation for the City to ensure that this information is tracked accurately because the City collects fees based upon the weight, volume or type of solid waste that is received or handled by any such operator, in order to recover the costs of the solid waste enforcement program authorized under Division 30 of the California Public Resources Code and implemented by the Local Enforcement Agency.

In the case of CWS, the Finance Department recently completed a routine compliance review and found that,

> *"CWS has reported and paid for solid waste tonnages from its permit date of March 18, 2005, to the current reporting month. Our review, however, has revealed that CWS has not reported, nor submitted the required SWEF for the solid waste tonnage that its San Jose transfer facility received and processed from March 4, 2003 to March 17, 2005."*

The total due to the City, and recently paid by CWS in August 2006, was $167,967.01. Additionally, the compliance review found "Inadequate or Improper Maintenance of Computerized Ticket Records" and suggested two recommendations to remedy this issue.

In addition to a financial obligation, the City of San Jose, through its solid waste collection and disposal contracts, is required to report to the California Integrated Waste Management Board (CIWMB) to demonstrate compliance with state mandated requirements related to solid waste diversion. The City is responsible for its landfill diversion requirements, but the ability to demonstrate compliance is dependent

on thorough and accurate documentation. If the documentation is not reliable, the City is not able to provide valid data to the CIWMB.

Consideration to Disqualify California Waste Solutions (CWS) from the RFP process

In the report dated August 10, Macias Consulting Group recommended that the City consider disqualifying CWS from the 2007 Request for Proposal process. Section 5.2 of the RFP, titled "Disqualification," states that "Evidence of incorrect information submitted as part of the proposal" may be considered just cause to disqualify a proposal without further consideration.

On May 31, the City informed CWS that the Technical Evaluation Committee will visit CWS's Material Recovery Facility in the morning of June 7. On June 2, the City's Building Inspector signed off on the Building and Electrical Permit for the installation of new glass processing equipment which means that the inspector determined that all permit requirements were complete and use of the equipment covered by the permit could commence.

On page 6 of the Macias report, it states that Macias was able to verify that 463.43 tons of unprocessed material (Mix-C Materials) were picked up and transported by American Recycling Services, a CWS vendor, between May 31 and June 7. The report continues to say that, "The last two outgoing loads of Mix-C Materials out of CWS' San Jose facility were at 12:19 and 12:39 a.m. on June 7, 2006 - just prior to the 9 a.m. proposal site visit."

Albeit, the City could corroborate CWS' reasons for the need to "clean-up" the Material Recovery Facility, CWS was not forthcoming in sharing with the City the removal of unprocessed material, as contractually obligated, or as a common business practice to promote integrity and honesty with Technical Evaluation Committees.

Since the Administration cannot determine with certainty the actions by CWS to remove over 450 tons of unprocessed material, which exceeds the daily volume of processing recyclables, violated Section 5.2 of the RFP, CWS' proposal will not be disqualified. The Administration is concerned that a delay in processing of recyclables caused by the installation of the glass processing equipment caused such a large disruption to the MRF which raises questions about CWS' ability to perform the obligations of the current contract with Norcal or any future contracts with the City.

Conclusion

The findings in both the Macias report and Finance Department's Compliance Review show that there is improper and/or inadequate tracking and reporting of materials entering and leaving CWS's San Jose site. Additionally, not only is the removing of unprocessed material in violation of the contract, the coincidence of the removal of such a large quantity, which started on the day the City informed CWS about the upcoming site visit, is troublesome. The reports clearly demonstrate that CWS has, on its own, violated provisions of the contract and performed inappropriately during the procurement process.

Les White
City Manager

Attachments:
(A) Correspondence from Archer Norris and CWS
(B) Macias Supplemental Report, dated August 16, 2006
(C) Department of Finance Compliance Review Findings

Attachment A

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August 7, 2006

VIA EMAIL

Walter Rossmann
Chief Purchasing Officer
City of San Jose
200 East Santa Clara Street
13th Floor
San Jose, California

Re: Tab 4, Exhibit 4, Award of Contracts for 2007 Recycle Plus Services – Protest Period and Investigation by the City's External Auditor

Dear Chief Purchasing Officer:

The purpose of this letter is to highlight the unlawful, discriminatory and unfair actions that are threatened by the City at Tab 4, Exhibit 4, Award of Contracts for 2007 Recycle Plus Services issued August 1, 2006, by the City of San Jose (the 'City"). The City's document states:

> The City of San Jose received copies of two letters, dated June 2 and June 7, sent to the California Waste Solutions (CWS) from the Business Representative for the Sanitary Truck Drivers and Helpers, Local No. 350. In their letters, the Teamsters alleged that CWS removed unprocessed recyclable material from the San Jose Materials Recovery Facility. The contract between Norcal and the City of San Jose, with CWS serving as a subcontractor for the processing of recyclable materials, stipulates that all processing of recyclable materials needs to occur at CWS' facility in San Jose, unless directed otherwise by the City. Since the Technical Evaluation Committee visited CWS' Material Recovery Facility on June 7 to assess CWS' operational capacity to process recyclable materials, Finance requested an independent audit to determine whether the removal of the recyclable materials compromised the procurement process and warrants disqualification of CWS' proposal. Additionally, the City asked Macias [its consultant] to determine whether City staff appropriately administered the current contract with Norcal and CWS as Norcal's subcontractor. The investigation is scheduled for completion by August 9. The results of the investigation will be issued to Council via a Supplemental Memorandum on August 14.

The City's announcement that it intends to release a report that may condemn CWS just days prior to the City Council's award of a contract is outrageous. The City's announcement is based on two letters from the Teamsters union.

To be clear, the City admits that it received letters from the Teamsters Union on June 2 and June 7, 2006 and that the City has waited well over two months - until just days prior to the scheduled City Council action on selection of a new contractor – to announce the results of its investigation.

We offer the foregoing so that the City can place the communication from the Teamsters in context. We offer it also as insight into the important role the Teamsters see for themselves in the award of a new contract. The history of Norcal, the Teamsters and the Environmental Services Department is one of excessive Teamster influence coupled with deception and, according to the Santa Clara County District Attorney, unlawful conduct by Norcal for the apparent purpose of serving the interests of the Teamsters. Recall that it was Carl Mosher wearing his hat as Director of ESD who delivered the deceiving report to the City Council in 2003 upon which the City Council was asked to raise garbage rates.

The unlawful attempt by the City, carrying the water of the powerful Teamsters once again, to get in a "late hit" by circulating results of an investigation at the very last minute effectively deprives CWS of the due process rights afforded under the RFP and to which CWS is entitled as a matter of law.

It is ironic that the allegations made by the Teamsters amount to nothing. CWS has explained at length to ESD that it is not precluded from selling mixed recyclables – which is precisely what CWS did. It is critical to note that ESD has had knowledge of the sale of mixed recyclables from reports prepared by CWS and Norcal for years and has never assessed a fine or declared a breach of the Recycle Plus Agreement because of the sales. It is only now, immediately prior to the selection of a new solid waste contractor, that the City insinuates that CWS acted improperly. The City's conduct – and especially the actions of the Environmental Services Department are unlawful and discriminatory.

The sale of mixed recyclables does not harm the City. On the contrary, under applicable law, the City is credited with having recycled the material. The loser in the transaction is CWS who suffers a severely reduced price for the materials sold as mixed. The economic reality of the recycling business is that CWS makes more money from sorting mixed recyclables into their constituent parts than from selling them in bulk – even after deducting the cost of the extra sorting required. CWS has sold small amounts of mixed recyclables over the years (1.4% of all outgoing materials) – reported to the City – when the level of contamination in the incoming material has slowed down plant operations. In that event, material is processed from the tipping floor and shipped out as mixed recyclables to avoid excessive inventories of material on sight.

CWS' sale of mixed recyclables did nothing to alter the operations of CWS' facility. The members of the TEC were able to watch material enter the facility, flow through the processing

equipment, into the balers and to storage. The City has records of all of the sales of recyclables, including mixed recyclables, going back over four years. The City knows that the total amount of mixed recyclables sold by CWS is extremely small and not material. It is outrageous that the City would, at the last moment, employ consultants to find CWS disqualified as a bidder based on a practice that has been known to the City for years and for which the City has never assessed a fine or declared a breach. Interestingly, the City did not advise bidders that it would not sanction the sale of mixed recyclables.

The City also notes that it "asked Macias to determine whether City staff appropriately administered the current contract with Norcal and CWS as Norcal's subcontractor." CWS notes for the record that no one at Macias made any inquiries of CWS employees regarding the administration of the current contract by the City. It is difficult to imagine that Macias could reasonably determine the quality of the City's administration of the current agreement absent an understanding of the communication between the City and CWS. The failure to inquire of CWS regarding the City's administration assures that the information available to the consultant is incomplete and any conclusions suspect. Again, CWS is not only denied due process with respect to the Teamster inspired, City implemented last minute smear, CWS is denied even the futile opportunity to explain its side of the story to the consultants.

This letter should not be considered to be CWS' "Protest" as provided in the RFP process but rather CWS' notice to the City of its concern regarding how the City intends to proceed over the next two weeks.

Thank you for your attention to these urgent matters.

Sincerely,

ARCHER NORRIS

By

Richard E. Norris

Attachment A

August 11, 2006

Walter Rossmann
Chief of Purchasing
City of San Jose
200 East Santa Clara Street
San Jose, California

Re: CWS Response to Macias Report

Dear Mr. Rossmann:

The Final Report of the Recycle Plus Procurement Process Review (the "Report") prepared at the direction of the City of San Jose (the 'City") by the Macias consulting group ("Macias") is the best evidence to date of the City's antipathy towards CWS and its apparent willingness to forsake both truth and common sense in its headlong effort to secure a contract extension and rate increase for its defacto partner, Norcal.

Macias, a firm without any apparent expertise in the field of solid waste beyond accounting, begins its hatchet job on CWS by declaring that:

> "CWS ***may have breached its current contract*** with Norcal Waste Management Systems by transporting 463.43 tons of unprocessed recyclable materials (Mixed C Commodity [hereafter, "Mixed C"]) between May 30, 2006 and June 7, 2006."(Emphasis added)

Logic compels that, even according to Macias, CWS may ***not*** have breached its contract with Norcal by shipping Mixed C. That is certainly the key issue in unraveling the web of deceitful slander that forms the core of this latest unfair and unlawful attempt to deny the 2007 Recycle Plus contract to the qualified low bidder, CWS, and, instead, create the false impression that the City has no choice but to continue to contract with Norcal who has undeniably lied to the City, who is indicted for the crime of bribery, who is subject to millions of dollars in unresolved fines assessed by the City, and who has failed miserably in cleaning up the recyclable material collected at the curb.

First, let there be no question about it. CWS has the right to sell Mixed C under its subcontract with Norcal and the sale of Mixed C is not a violation of the Recycle Plus agreement. Even Macias admits in their Report that there have been "sales" of Mixed C over the years. Sales to which the City never raised a single objection until now, at the eleventh hour of the procurement process.

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Macias offers no explanation for why it refers to "sales" of Mixed C before May 30, 2006 (page 6 of the Report) but recharacterizes precisely the same transaction as "transport[ing] material outside of City limits without processing" when it addresses the same factual situation for the period May 30 through June 6, 2006. The reason appears to be that if Macias acknowledges the obvious truth that the sale of Mixed C is not a breach of contract by CWS, its last minute hatchet job on CWS collapses like a house of cards. Because the sale of mixed recyclables is not a breach of contract. So CWS did nothing wrong.

The proof that sales of Mixed C do not violate the Recycle Plus agreement is:

1. There is no language in the Recycle Plus agreement that precludes the sale of mixed recyclables. That should be enough. But there is more.

2. CWS undertakes minimal processing of Mixed C when it is sold by performing a simple floor sort, excluding as much of the obvious contaminants as possible as the material is loaded from the sorting floor of CWS into trucks.

3. Mixed C is not processed in Oakland by ARS or anywhere else. Instead, it is baled and sold AS IS into the recycling markets in Asia where it is turned into products (and probably sold back to the United States in the form of plastics, metal and paper products).

4. For the past four and one half years CWS has periodically sold Mixed C and reported that fact to the City. The City's acceptance of CWS's practice is excellent evidence of the fact that the City admits that the sale of Mixed C is allowed under the Recycle Plus Agreement.

5. Macias does not even attempt to distinguish between authorized sales of Mixed C that have taken place over the years and the allegedly illegal sales of Mixed C in May and June of this year.

6. Macias fails to offer any insight whatsoever into the commercial reasonability of the sale of Mixed C and cannot offer competent insight due to its fundamental lack of expertise in the solid waste field. Is it not relevant that the sale of mixed recyclables is commonplace in the recycling industry? Is it not relevant that the City hired consultants who are not capable of bringing this important fact to the attention of the City?

It is every bit as interesting to consider the issues that the City did not employ Macias to investigate as it is to consider the Macias Report. In a kind of "through the looking glass" process, the City spends its time, effort and resources delivering a last minute hit piece against CWS that is fundamentally flawed while, at the same time, leaving unexplored the following matters that deserve investigation and comment:

1. Should the City enter into a contract with Norcal? Did Norcal lie to the City about its rate increase of $11,000,000? Is Norcal guilty of a crime? Does Norcal complicity in the 2003 rate increase and 2004 payments to Norcal disqualify Norcal from being a City contractor?

2. Did the City have reliable waste characterization data as early as 2003 regarding contamination in the materials received by CWS from Norcal? Did ESD lie to the City Council and to bidders when it has denied the existence of waste characterization data?

3. Should Norcal be disqualified as a bidder because it failed to reduce the level of contamination in the recyclables it picks up in San Jose to below 10%?

4. Should Norcal be disqualified as a bidder because of the $10,000,000 in fines pending against Norcal?

5. Was the procurement process fundamentally undermined by the City's disingenuous request for bids for a two-year term when the City knew full well that the only bidder who could possibly undertake a two-year contract is Norcal?

Each of the foregoing issues is far more fundamental to the procurement process than whether or not CWS sold Mixed C. Yet the City leaves all of these questions unanswered. .

The Report acknowledges that the members of the TAC who visited the CWS facility knew that the facility had been notified of the visit and, presumably, the members of the TAC understood that CWS made every effort to demonstrate its capabilities.

When the TAC was present on the CWS site, materials were processed in the ordinary course of business. The prior sale of Mixed C did nothing to adversely impact the ability of the TAC to inspect the processing capability of the equipment on the floor of CWS. Macias seems to argue, though it does not come out and say it, that the sale of Mixed C undermined the ability of the TAC to see CWS process material through its plant. This argument is ridiculous. CWS has operated for four and a half years as the sole and only processing facility for the material collected by Norcal. CWS has sold less than 1.4% of the material it receives from Norcal as Mixed C. CWS has processed all of the material it has received. What more proof need one present? Without experience in the business of processing recyclables, Macias is unable to offer any reasonable opinion of the effect of the sale of Mixed C on the ability of the TAC to judge CWS' performance.

Macias attacks CWS for cleaning up its facility in preparation for the TAC visit while Macias is silent on the fact that Norcal does not even have a recycling facility capable of operating for the 2007 contract. The City and Macias studiously avoid addressing the real issue - how Norcal expects to secure a solid waste facility permit and equip its empty truck parking facility to process hundreds of tons of contaminated recyclables per day in time to implement the 2007 Recycle Plus Agreement. Nor does Macias explain why a solid waste facility permit was not required in the RFP in light of the fact that the material collected by Norcal contains over 20% garbage – requiring a solid waste facility permit for handling.

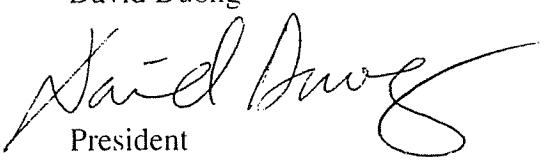
It is important to note that CWS was selling Mixed C in late May, 2006, before CWS was notified of the TAC's visit. CWS has explained that those sales were occasioned by the fact that CWS was testing new glass processing equipment. CWS has explained that it is economically disincented from selling Mixed C because the price of Mixed C is lower than the difference

between the price of segregated materials and the cost of segregating them. The price for Mixed C is from $25.00 to $30.00 per ton. The average value of segregated materials is in the range of $125.00 per ton. The cost of processing is in the range of $50.00 per ton.

Macias spends several pages expressing its uncertainty over the tonnage of Mixed C sold by CWS in May and June. The answer is simple. The weigh tags generated as material leaves the Timothy Street facility foot exactly to the Outgoing Material Reports provided by CWS to the City. Macias makes the "rookie" mistake of comparing invoices for sold material with weigh tags and the Outgoing Tonnage Reports. If Macias had experience in the recycling business, Macias would know that discounts on the sale of recyclables often are given by reducing the tonnage rather than the price – maintaining the fiction in the market place that the invoice price reflects the market. Macias' ad hominem attack on CWS' accounting practices with respect to Mixed C is really Macias' admission of its ignorance of the industry that it was paid to audit. Macias' inexperience is excusable. The City's and Macias' failure to qualify their findings by explaining their limited knowledge of the field is not.

CWS registers its sincere outrage and disappointment with the City's and Macias' over the top last minute hit piece. CWS reminds the City that it collects from 70,000 homes per week under its Oakland contract and that the Director of Public Works in Oakland finds CWS to be "excellent." The fact that the staff did not advise the City Council of the Oakland Director of Public Works high opinion of CWS' competence is one more remarkable omission suggesting both incompetence and prejudice against CWS. CWS urges the City to reject the Macias Report as the poorly researched and unfairly motivated tract that it is and to select CWS as the qualified low bidder best able to provide excellent service to Districts A and C.

David Duong



President
California Waste Solutions, Inc.

MACIAS

CONSULTING GROUP

August 16, 2006

Mr. Walter Rossmann, CPM
Chief of Purchasing
City of San Jose
200 East Santa Clara Street
San Jose, California

RE: Macias Response to CWS Comments and Response to Macias Report

Dear Mr. Rossmann:

On July 21, 2006, Macias Consulting Group contracted with the City of San Jose (City) to assess the validity of claims that California Waste Solutions (CWS) transported recyclable materials outside of City limits prior to a site visit conducted by City staff in connection with the City's current RFP process for a new solid waste contract. The City currently prohibits the transporting of unprocessed recyclable outside of City limits unless authorization is granted by City officials.

On August 10, 2006, Macias Consulting Group, Inc. submitted its report of agreed upon procedures to address the aforementioned issues. On August 11, 2006 CWS submitted their response to our report.

The purpose of this letter is to address specific comments presented by CWS in response to our report.

1. CWS Comment (In response to the second paragraph, second page of the bid protest regarding the timing and manner of implementation of Macias to consider CWS' disqualification): "The City delayed action on the allegations upon which the Macias engagement is allegedly based for nearly two months, the City acting through its Purchasing Department and the RFP process coordinated its investigation with CWS' Competitor, Norcal, who actually arranged for the initial conference between CWS and Macias. The unauthorized contact between Macias and Norcal regarding the efforts to disqualify CWS is fundamentally unfair."

Macias Response: Our review of the procurement process for the 2006-2007 Recycle Plus contract bid did not place CWS at a competitive disadvantage. Our review began

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after the City had made considerable progress in evaluating potential bidders and the City had made a preliminary decision to go with Norcal prior to our completion of the review.

Second, our interaction with Norcal primarily focused on the coordination and collection of data that we needed to carry out our review. Because Norcal was the prime contractor under the existing contract, we were obliged to send them our initial data request to help determine what information Norcal had available for us to review to avoid making a duplicate request to CWS. Also, we requested Norcal to set up a joint teleconference call with Norcal, CWS and our firm to discuss our initial data request. This meeting was arranged by Norcal for 2PM on July 26, 2006. After repeated attempts by Norcal to reach CWS officials to participate in this meeting, our firm opted to begin the meeting with Norcal officials to specifically identify the extent of available information. After this meeting, Norcal provided our firm with the contact names and phone numbers of CWS officials so that our firm can arrange another meeting to discuss the same data documentation request. This subsequently was held about 30 minutes later when our firm successfully contacted CWS officials who reported that they had been waiting for our call. CWS officials then requested to reschedule the meeting so that Norcal officials could be involved since they were the prime contractor, but we explained that it was not necessary for them to participate in this meeting with CWS to discuss data needs. CWS agreed. As a result, given the limited interaction that we had with Norcal, we believe that CWS was not placed at a competitive disadvantage.

Finally, CWS questioned the timing and manner of implementation of our review. We were contacted and engaged in a contract to begin the review on July 21, 2006, and began work immediately. We were contractually obligated to complete the draft report by August 9, 2006. The manner of our implementation was carried out in accordance with generally accepted governmental auditing standards. We did request an onsite interview with CWS officials so that we could ask questions pertaining to the results of our review, but CWS officials did not contact us until a day before the report was due. As a result, we requested that CWS officials respond to our questions via e-mail. This was an appropriate action given the timeline of our review.

2. CWS Comment: Macias, a firm without any apparent expertise in the field of solid waste beyond accounting, begins its hatchet job on CWS by declaring that: "CWS may have breached its current contract with Norcal Waste Management Systems by transporting 463.43 tons of unprocessed recyclable materials between May 30, 2006 and June 7, 2006".

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CONSULTING GROUP

Macias Response: Our firm has extensive experience dealing with solid waste issues. In the past five years, our firm has performed 37 engagements related to solid waste management. These reviews covered a myriad of topics from developing alternative solid waste recovery methods, to establishing tipping fees. Please See Attachment A for a full client list of solid waste management analyses and studies.

3.CWS Comment: Logic compels that, even according to Macias, CWS may not have breached its contract with Norcal by shipping Mixed C.

Macias Response: Our review focused on whether CWS took appropriate actions in the RFP procurement process by cleaning the site of recyclable materials. As stated in our report, there is sufficient testimonial evidence to substantiate that the extent of the clean up performed was not typical of day-to-day operations of the facility. City contract management officials, Norcal officials, and evaluation panel members reported the CWS facility is routinely at capacity to the extent that trucks are lined up outside of the facility waiting to tip their load. During the site visit, no excess materials were noted on the tipping floor by evaluation panel members. As a result, the extent that CWS cleared the site of recyclable materials would appear to contradict information provided by CWS that it could handle its current capacity as well as the additional capacity expected with the new contract. Section 5.1 of the Recycle Plus RFP cites evidence of incorrect information submitted as part of the proposal may be grounds for disqualification.

Additionally, we suggested in our report, that City officials should consider requesting Norcal to cancel its subcontract with CWS. Section 7 of CWS' contract with Norcal states that CWS acknowledges that failure by CWS to process residential recyclable materials could constitute a breach.

4. CWS Comment: CWS has the right to sell Mixed-C under its subcontract with Norcal and the sale of Mixed –C is not a violation of the Recycle Plus agreement. Even Macias admits in their report that there have been sales of Mixed C over the years.

Macias Response: Macias does not dispute CWS' right to sell Mixed-C, rather our review examined whether the shipments of the material prior to sale were authorized to be transported out of City limits for processing, which is a contractual requirement. We did note CWS had not sold Mixed-C materials since July 2005 when 14.87 tons were sold compared to the 463 tons that were sold between May and June during the time of the proposal site visit.

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5. CWS Comment: Macias offers no explanation for why it refers to "sales" of Mixed C before May 30, 2006 but re-characterizes the same transaction as transporting material outside City limits without processing when it addresses the same factual situation for period May 30 through June 6, 2006. The reason appears to be that if Macias acknowledges the obvious truth that the sale of Mixed C is not a breach of Contract by CWS, its last minute hatchet job on CWS collapses like a house of cards. Because the sale of mixed recyclables is not a breech of contract. So CWS did nothing wrong.

Macias Response: CWS is referring to two separate sections where we delineate between that which we could determine was sold and then what we could determine was transported/shipped, – two separate issues. First we point out the tonnage on record that was sold compared to the outgoing tonnage report showing the amount shipped, where both were sold and shipped by ARS, yet the tonnage amounts were inconsistent. Finally, we reported the July 2005 sale because it was an uncommon practice by CWS to sell the Mixed-C materials. We concur with CWS' response, that the actual "sale" of these materials does not constitute a breach of contract, rather obtaining permission from the City through Norcal is a contractual requirement and would have alerted the City during the procurement process that this level of activity had taken place.

6. CWS Comment: Macias does not even attempt to distinguish between authorized sales of Mixed C that have taken place over the years and the allegedly illegal sales of Mixed C in May and June of this year.

Macias Response: Our report discusses the unauthorized shipment of recyclable materials between May and June of 2007 and does not make mention of any illegal sales of Mixed C. We did point out errors in invoicing procedures and questioned the accuracy of the amount CWS reported as being sold.

7. CWS Comment: Macias fails to offer any insight whatsoever into the commercial reasonability of the sale of Mixed C and cannot offer competent insight due to its fundamental lack of expertise in the solid waste field. Is it not relevant that the sale of mixed recyclables is commonplace in the recycling industry? Is it not relevant that the city hired consultants who are not capable of bringing this important fact to the attention of the city?

Macias Response: The commercial reasonability of the sale of Mixed C was not within the scope of this review. We implemented the procedures outlined in our report solely

for the purpose of assisting the City in evaluating the integrity of the current RFP process for a new solid waste contract.

8. CWS Comment: Macias attacks CWS for cleaning up its facility in preparation for the TEC visit while Macias is silent on the fact that Norcal does not even have a recycling facility capable of operating for the 2007 Contract. The city and Macias studiously avoid addressing the real issue – how Norcal expects to secure a solid waste facility permit and equip its empty truck parking facility to process hundreds of tons of contaminated recyclables per day in time to implement the 2007 Recycle Plus Agreement. Nor Does Macias explain why a solid waste facility permit was not required in the RFP in light of the fact that the material collected by Norcal contains over 20% garbage requiring a solid waste facility permit for handling.

Macias Response: As stated in our report, we found CWS' cleanup of its site to be a reasonable action prior to the TEC site visit. We reported that the extent that CWS cleaned up the site contradicted information provided by CWS in the proposal process that it has sufficient capacity to handle the processing of recyclable materials. Additionally, our review focused on four objectives related to vendor and City actions taken in the current RFP process. Examining Norcal's capacity for handling recyclable materials were subsequently not part of this review.

9. CWS Comment: It is important to note that CWS was selling Mixed C in late May 2006, before CWS was notified of the TEC's visit. CWS has explained that those sales were occasioned by the fact that CWS was testing new glass processing equipment. CWS has explained that it is economically dis-incented from selling Mixed C because the price of Mixed C is lower than the difference between the price of segregated materials and the cost of segregating them.

Macias Response: On August 4, 2006 we contacted CWS officials for an explanation on why Mixed C materials were sold in May and June 2006 when there was no other record of the Mixed C sale in the past. CWS responded on August 9 after a second contact to appropriate officials to obtain a response. Our firm did not receive a direct and adequate response or explanation by CWS officials as to why Mixed C materials were sold in this timeframe. We examined this most recent explanation by CWS indicating that the sale of the materials was due to testing of new glass processing equipment. We found that CWS did install new glass processing equipment for its San Jose facility in May 2006, so we continue to question why Mixed C was sold and transported to the Oakland facility during the timeframe of the site visit (May, June 2006).

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10. CWS Comment: Macias spends several pages expressing its uncertainty over the tonnage of Mixed C sold by CWS in May and June. The answer is simple. The weigh tags generated as material leaves the Timothy Street facility foot exactly to the Outgoing Material Reports provided by CWS to the City. Macias makes the "rookie" mistake of comparing invoices for sold material with weigh tags and the Outgoing Tonnage Reports. If Macias had experience in the recycling business, Macias would know the discounts on the sale of the recyclables often are given by reducing the tonnage rather than the price – maintaining the fiction in the marketplace that the invoice price reflects the market. Macias' ad hominem attack on CWS' accounting practices with respect to Mix C is really Macias' admission of its ignorance of the industry that it was paid to audit. The City's and Macias' failure to qualify their findings by explaining their limited knowledge of the field is not.

Macias Response: CWS' weight tags and the data reported in CWS' Outgoing Material Report do not reconcile. Thus, this is at the heart of our concern over data discrepancies among the various sources of data received by CWS. According to CWS Weight Tickets, and the corresponding CWS Outgoing Tonnage Reports from the CWS' San Jose facility, we found that between May 31, 2006 and June 7, 2006, 33 truck-loads totaling 463.44 tons of Mixed C recyclables were transported by the vendor, ARS. However, another CWS quarterly report submitted to Norcal showed 497.10 tons of Mixed C shipped and sold in May and June 2006. We were unable to reconcile the difference of 34 tons.

During our course of our review we contacted one of the largest and most reputable solid waste management companies in the nation and they reported that it is not a standard practice to alter tonnage on invoices. As outlined in our report, we adhere to our original position that we would have expected to see, at a minimum, the same tonnage shipped but at a reduced price, with any discounts properly noted on the invoice.

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MACIAS
CONSULTING GROUP

Attachment A: Macias Consulting Group, Inc.
Solid Waste Management Analyses Experience

The following clients represent our experience with solid waste management analyses and studies:

Municipal Solid Waste Clients

- City of Fresno
- City of Modesto
- El Dorado Sanitation District
- Santa Clara Valley Water District
- County of Mendocino
- County of Tuolumne
- County of Yolo
- City of Galt
- City of West Sacramento
- County of Butte

Waste Management and Landfill Organizations

A & A Recycling Systems
Amador Disposal Service
American Avenue Landfill
American River Disposal
California Integrated Waste Management Board
Camarillo Waste Removal, Inc.
CWRS
Eastern Regional Landfill
El Dorado Disposal Service, Inc.
El Dorado Landfill, Inc.
Jamestown Landfill
Neal Road Sanitary Landfill
Orange County Integrated Waste Management Department
Refuse Enterprise Fund of the County of Sacramento
Riverside County Waste Management Department
Sacramento County Sanitation District No. 1
Sacramento Regional County Sanitation District
Sacramento Valley Environmental Waste Disposal Company
Sierra Disposal Service
South Napa Waste Management Authority
South Tahoe Refuse Company, Inc.
Tahoe Truckee Disposal Company
Tri-C Waste Disposal Division; and Waste Management of Sacramento
Union Mine Landfill
Upper Valley Waste Management Agency
Waste Management of Sacramento
Western Placer Waste Management Authority

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Attachment C

CITY OF SAN JOSE
CAPITAL OF SILICON VALLEY

Finance
SCOTT P. JOHNSON, DIRECTOR

July 21, 2006

David Duong, President
California Waste Solutions, Inc.
1005 Timothy St
San Jose CA 95133

Re: Results of Compliance Review of California Waste Solutions, Inc. (CWS)

Dear Mr. Duong:

The compliance review of California Waste Solutions has been completed. Our review focused specifically on CWS's compliance with the municipal code pertaining to the payment of Solid Waste Enforcement Fees (SWEF).

As explained in our letter (see attached copy) dated May 22, 2006, the compliance review period was extended to a maximum of three years and covered the period March 4, 2003 to March 4, 2006. Limited testing was used to determine the accuracy and reliability of information that CWS provided us, and our findings are as follows:

Finding 1 – *Unreported and Unpaid Tonnages (Financial)*

CWS has reported and paid for solid waste tonnages from its permit date of March 18, 2005, to the current reporting month. Our review, however, has revealed that CWS has not reported, nor submitted the required SWEF for the solid waste tonnages that its San Jose transfer facility received and processed from March 4, 2003 to March 17, 2005.

The SWEF for these unreported solid waste tonnages is required to be paid whether or not a solid waste facility has a permit as clearly stated in San Jose Municipal Code Section 9.10.570, which is excerpted below:

> *"Any person who engages in such business or activity without the required authorization shall nevertheless pay to the city, and be liable to the city for, the amount of any tax, fee or other charge required to be paid by other provisions of this chapter for the privilege of engaging in such activity ."*

The total assessment from this finding is **$167,967.01,** which includes penalty and interest calculated through July 15, 2006. Computation of penalty and interest is set forth in Section 9.10.960 D, E and G of the code. To resolve this finding, the total assessment must be paid in full.

Finding 2 – *Inadequate or Improper Maintenance of Computerized Ticket Records (Non-financial)*

(i) Tickets issued for incoming tonnages were subsequently voided. The reviewer could not determine if these were canceled or corrected transactions. While some canceled transactions may not require replacements, the opposite is true for corrected transactions. Since the reasons for voiding these transactions were not indicated on the list that was submitted to us, it was not possible to determine if replacement tickets were ever issued especially for those transactions that were corrected later.

Recommendation: These voided tickets were accepted as is for this compliance review; however, CWS needs to provide adequate information on all future incoming tickets that may be voided, and on the corresponding replacement tickets.

(ii) CWS uses a company-wide automated ticket system, which is programmed to generate a sequential ticket number for incoming tonnages for all facilities, including the two located at Oakland, California. Since CWS is only responsible for paying the SWEF for incoming tonnages at its San Jose transfer facility, the tickets for incoming tonnages issued in Oakland would appear to be unreported in San Jose or vice versa. To verify if the City received the appropriate SWEF for all incoming tonnages, staff expanded its review to include the tickets issued by CWS's Oakland transfer facilities.

Recommendation: To avoid the increased burden of producing and reviewing additional documents on both CWS and the City, it is recommended that CWS should re-program its automated ticket system to generate a unique sequential ticket number for each location.

Total Assessment

Based on the findings indicated herein, a total of **$167,967.01** is currently due and payable to the City. Please remit your payment by August 4, 2006.

The City values its relationship with California Waste Solutions, Inc. and looks forward to resolving this matter. If you have questions or require additional information, please contact Mark Brogan, Financial Analyst at (408) 535-7092.

Sincerely,

SCOTT P. JOHNSON
Director, Finance Department

Enclosures
Cc: Mark Rasiah, Acting Deputy Director Finance
Mark Brogan, Financial Analyst