Participation in the Consultation on the Circular Economy Act

Introduction

ARERA thanks the Commission for the appreciable opportunity granted to citizens, institutions and stakeholders to attend in the discussion preliminary to the formation of new measures to support community policies on circular economy. This note, which ARERA sends to the attention of the Commission, as a supplementary contribution to the online survey, reports the main recommendations on the topics of competence and, in particular, how regulation can contribute to promote circular economy.

ARERA'S role in the context of municipal waste sector (MWS)

The Italian Regulatory Authority for Energy, Networks and Environment (ARERA) carries out regulatory and supervisory activities in the sectors of electricity, natural gas, water services, waste cycle and district heating. Established by Law no. 481 of 1995, ARERA is an independent administrative authority that operates to ensure the promotion of competition and efficiency in public utility services and protect the interests of users and consumers. These functions are performed by balancing operators' economic and financial objectives with general social objectives, for environmental protection and the efficient use of resources.

Law no. 205 of 2017 has attributed to ARERA the tasks of the regulation and control of the cycle of urban and similar waste "*for the purpose of improving the waste cycle regulation system, including recycling, urban waste and similar, in order to guarantee homogeneous accessibility, usability and distribution throughout the country, as well as adequate levels of quality in terms of efficiency and low costs of management, harmonising the economic/financial objectives with the general social and environmental objectives and those of the appropriate use of resources, in addition to guaranteeing the infrastructural compliance with European regulations, thus overcoming the infringement procedures already in motion, with consequent economic benefits for the local authorities affected by said procedures*".

Italian MSW has a complex multi-tier governance structure with direct or indirect involvement of all municipalities even at different decentralized levels. Specifically:

at national level:

- macro-objectives are established, in line with Community legislation, by the State (through the Ministry of Environment);
- ARERA has the power to establish rules valid for the whole national territory in terms of tariff *criteria*, quality of services and transparency, consumer protection;

at local level:

- Regions define the optimal territorial areas (also called ATO, usually at regional or subregional scale) in which waste services are organized and constitute a local legal entity for the management of each optimal area (called EGATO or ETC);
- EGATO or ETC (which usually has a regional or provincial size) is responsible for organizing waste services in its relative ATO, provides for the assignment of the

service to operators (choosing the appropriate institutional form, i.e. in-house, IPPP or tender procedures), defines, on the basis of the *criteria* set by ARERA the financial economic plans to set the operator tariff revenues;
- Municipalities must take part to EGATO; in some cases, contribute to operating activities (e.g. billing/pricing).

How regulation can contribute to Circular Economy

The Circular Economy Act (CEA) is one of the main objectives of the new Commissioner for the Environment; the Commission's commitment is to start work on the CEA in 2025, so to present a legislative proposal by 2026. The Commission aims to reinforce the single market for waste and secondary raw materials, increasing the supply and demand of quality secondary raw materials at competitive prices, and 'getting the economics right' for these markets.

The need for organic action and strong change arises from the awareness of the slowness of the process of pushing the economy towards circularity driven by several regulatory and market failures as:

- heterogeneous interpretations and implementation of EU rules by Member States that create a fragmentation of the single market, making it costly for businesses to convert waste into valuable secondary raw materials and preventing economies of scale;
- higher prices of secondary raw materials due to fact that they do not reflect their lower environmental impacts;
- risks of information constraints and asymmetries, behavioural biases, transitional costs and risks of fraud for consumers and sellers of secondary raw materials;
- unaccounted waste streams and 'leakages' of secondary raw materials, including critical raw materials, lead to mixed or 'incorrect' waste streams being incinerated, landfilled and (illegally) exported.

Based on the context outlined above, the Commission intends to structure CEA's interventions on the basis of two main pillars:

- ensure effective collection and recycling of e-waste (that are the fastest growing waste stream of which less than 40% is recycled) and to generate market demand for the secondary critical raw materials;
- mix of interventions to foster the single market for waste, secondary raw materials and their use in products (as reform of end of waste criteria; simplification, digitalisation and extension of extended producer responsibility schemes; setting mandatory, targeted, impactful, and implementable criteria for public procurement of circular goods, services and works to stimulate EU demand).

With regard to these goals, the regulatory principles can support the path towards the circular economy paradigm, in particular setting: tariff rules, service quality levels and citizens' engagement and protection mechanisms.

An important feature of national regulatory frameworks is the focus on cost efficiency, where **tariff** rules aim to:

- promote the achievement of environmental objectives in line with the EU and national frameworks, such as, for example, increasing levels of re-use and recycling;
- ensure the cost accountability and transparency, capping the possible overall growth in tariff revenues, for example through a limit to the annual increase of the tariff;
- improve the overall efficiency of operations promoting technological and process innovations in the context of a multi-year financial planning;
- maximize the revenues from the economic potential of the circularity, also using revenue sharing mechanisms between the industrial operators and the citizens;
- increase the focus on the infrastructural profile of the sector, starting from an exhaustive representation of the gap for waste treatment services to promote a more balanced configuration in terms of possible environmental and economic benefits of energy and material recovery, also incentivizing technological innovation and operational efficiency within the integrated waste cycle.

Regarding **quality**, regulators are committed to increase levels of quality of services, as well as the right of citizens to have homogeneous minimum levels of quality regardless of income and social background. The regulatory framework could include key indicators concerning technical, environmental and/or contractual performances in order to promote the achievement of targets in line with the EU and national frameworks, and to measure the different situations within the Member States and make them comparable, thus promoting the improvement of the outputs related to a single operator during a selected period.

Last but not least, in the MWS regulatory mechanisms consider citizens' double role of initial producers of the waste and individuals entitled to pay for its management. On one hand, citizens need to be properly informed and engaged, since their choices and behaviours contribute to an efficient waste management, and on the other they should be protected through affordable tariffs and adequate service quality levels. The disclosure of cost articulation and services' performances could enable the citizens' awareness and proactivity.

The role of the regulatory framework in providing circular resources for the industry

More specifically on separate waste collection activities, it is worth to notice that, by unanimous recognition, the quality of the output assumes an essential contribution to increase circularity: properly selected materials and developed infrastructures/plants for the management should deliver affordable inputs for the manufacturing activities. According to this view, regulatory stimulus to increase the quality of sorted waste could positively affect the competitiveness of the recycling industry, whose costs increase as the quality of recyclable waste decreases and the process scraps landfilled.

To increase the performance of sorted collection, regulation has introduced specific tariff rules to stimulate process improvements and use of innovative technologies. According to this approach, the Italian regulatory framework for the municipal waste takes into account all the relevant environmental performances. In particular, tariff revenues depend on actual service improvements and on provisional costs aimed at the achievement of the environmental EU targets; quality regulation also provides technical indicators in order to

evaluate the effectiveness in collecting and recycling activities, making performances comparable across different areas and pointing out the key factors of the waste services.

The holistic approach to waste management enables a joint evaluation of the contributions of each phase of the supply chain to the environmental performance. ARERA has introduced a specific indicator (called "R3") aimed to evaluate the environmental impact of the entire MW management in terms of CO2 emissions equivalent - with reference to the impact of separate waste collection, transport and treatment, the latter both in terms of the adopted treatment option (i.e. landfill, waste-to-energy plant) and of the technical efficiency and technological innovation of the plant park used. The indicator could enable the introduction of individual annual targets for each specific MW management area and/or yardstick and sunshine regulation mechanisms, and the evaluation of best practices and tools to minimize the environmental externalities. Specifically, R3 aims to:

- improve the quality of MW destined to recycling, reducing losses and inefficiencies;
- foster the use of sustainable vehicles for MW collection and transport to treatment plants and promote the minimisation of distances between the place of collection and treatment plants according with national framework that supports self-sufficiency and proximity specially for residual and organic MW;
- encourage the choice of the best treatment option, according to waste hierarchy principles and national waste management program, and technological innovation.

To elaborate a consistent regulatory framework, ARERA has intercepted these elements also in the process of defining the standard tenders' framework, including in the technical offer awarding criteria as:

- improvement of the separate collection and reuse objectives compared to the tender;
- development of collections dedicated to specific waste flows;
- improvements of ARERA's indicators aimed to increase, e.g., sorted collection performance;
- innovations aimed, e.g., at minimizing the environmental impact of waste transport (in terms emissions' reduction), or at the rationalization of collection, transport and sweeping activities, improvement of recycling rates, as well as at the contribution to critical raw materials' recovery.

Moreover, ARERA has been entitled by the national law to set the efficient costs to be covered by EPR packaging schemes (in force of the Directive (EU) 2018/851 that introduced obligation for producers to bear financial responsibility for the management of the waste stage of a product's life cycle including separate collection, sorting and treatment operations) and consequently, since 2024, has implemented a system to monitor and foster the gradual improvement of coverage degree of efficient costs of sorted waste collection, related to annual objectives and penalties (index H), with purpose to promote a gradual improvement of the fees received by producers' organizations (i.e. *Consortia*) for collective compliance with EPR obligations and the reduction of sorted waste collection and transport costs, which include indivisible operating costs and capital costs. In this field, ARERA takes part to a task force chaired by Minister of Environment for the supervision and control of the proper functioning of EPR schemes in Italy.

ARERA has defined the guidelines for accounting and administrative unbundling with the aim to promote cost accountability and efficiency in the MW management (also for the purposes of a correct disaggregation of costs eligible for tariff recovery) and competition (avoiding cross-subsidies).

Finally, it is worth to underline that the achievement of these goals needs an adequate planning capability at institutional level, which requires the improvement of the accountability of the local level of governance. The heterogeneity of the governance (regional – sub-regional or lower limit in ATO's border) with a great fragmentation at local regulatory level could represent an obstacle to the efficient implementation of the regulation and a limit for the deployment of its benefits for the citizens.