OUTER HOUSE, COURT OF SESSION

[2023] CSOH 41

P803/22

OPINION OF LORD YOUNG

in Petition of

ABDUL MAJID & SON LIMITED

Petitioner

for

Judicial Review of the Determination of the Return Handling Fee dated May 2022 in relation to Scotland's Deposit and Return Scheme

Petitioner: O'Neill KC; Welsh; TLT LLP
Respondent: Lindsay KC; Addleshaw Goddard, acting for Circularity Scotland Limited

30 June 2023

Issue

[1] This petition concerns an aspect of the Deposit and Return Scheme (DRS) shortly to be introduced in Scotland. The two issues raised in the petition are (i) whether the respondent is entitled to set the "reasonable handling fee" (RHF) payable under the DRS, and (ii) what factors must be taken into account in setting this fee.

Background

[2] The DRS is a scheme for the return of single use drinks containers sold within Scotland. The statutory power for the implementation of the DRS can be found in section 84 of the Climate Change (Scotland) Act 2009 which enables the Scottish Government to

establish by regulations a deposit and return scheme. The DRS has been established by virtue of the Deposit and Return Scheme for Scotland Regulations 2020 (SSI 2020/154).

[3] A brief description of the DRS is necessary to understand the issues in this case. The basic structure of the scheme is that single use drinks containers sold in Scotland will become subject to a 20p deposit. Each container's packaging will be marked to make clear that return of that packaging will enable the consumer to recoup the deposit. The consumer can return the packaging and collect their deposit at any return point. Most retailers of these drinks containers will be obliged to operate a return point. The aim of the scheme being that it should be as easy for the consumer to return the empty container as it is to buy the original product. A retailer operating a return point is termed a return point operator (RPO). The RPO may acquire a reverse vending machine for their premises which will enable the collection and storage of packaging to be automated, or the RPO may operate a manual, over-the-counter collection service. Producers of the packaging must arrange for the collection of their scheme packaging from each RPO. The producer is obliged to pay to the RPO both a sum equal to the deposit which has been returned to the consumer and a RHF for each item of scheme packaging collected.

[4] Sections 85 and 86 of the 2009 Act and regulations 13-15 of the 2020 Regulations allow for the creation and approval of a scheme administrator. It was anticipated that individual producers would seek to fulfil many of their obligations under the DRS through the medium of a scheme administrator. The respondent is a private company limited by guarantee formed to act as scheme administrator and it remains the only approved scheme administrator for the DRS. A Membership Agreement dated 22 February 2021 between the respondent and its founding members regulates the operation of the respondent and its relationship with its members. The founding members include a number of the most

significant producers of single use drinks containers in the Scottish market as well as certain trade associations. Other producers and RPOs may request to become members of the respondent but are not obliged to do so.

[5] The DRS was originally scheduled to commence in August 2023. Since the substantive hearing in this case, the Scottish Government has announced a delay in the commencement of the scheme until October 2025.

[6] The petitioner is a limited company which operates a retail convenience store, food outlet and post office between Bellshill and Coatbridge known as Baba's Kitchen and Costcutter. The premises comprise approximately 2,500 square feet of retail selling space. The petitioner participated in an early trial of a form of reverse vending machine in 2019. The sole director of the petitioner, Mr Majid, was also part of a delegation from the Scottish Grocers' Federation which visited Norway and Estonia to study the use of reverse vending machines in operation.

The decision under challenge

[7] The decision challenged in the petition is a determination of the respondent made in May 2022 and set out in a briefing document. The relevant part of the briefing document states:

> "The board is pleased to announce that they have reached a determination on the value of the RHF and is today issuing these fees to industry.
>
> Fees
>
> The RHFs for the first year of operation of the scheme are as follows:

Type of RHF	Fee/returned scheme article	Notes
Manual	2.69p	
Automatic (for those RPs utilising an RVM that complies with the CSL RVM specification)	3.55p for the first 8,000 containers received in each week by the RP 1.35p for each additional container received in each week by the RP	
Closed loop hospitality	0.13p	
Takeback	TBD	More details will be released in due course

[8] The briefing note explained that the level of the RHF had been calculated by an independent entity, PwC, who had been appointed as RHF consultant. In relation to the methodology used by PwC, the note explained:

> "The RHF consultant developed a detailed cost model aligned to the requirements of the regulations. Data to populate the model was sourced from the broad range of RPOs that will operate in Scotland, and augmented with and validated by input from other operating schemes around the world (where appropriate), and major independent reference points and indices. The model is designed to reflect the variation in costs across different types and sizes of RPOs and materials".

[9] In the period between service of the petition and the substantive hearing on the petition and answers, the respondent issued a RHF review report dated January 2023. The review report made no change to the RHF for manual and takeback but did raise the two fee levels for automatic from 3.55p to 3.7p, and from 1.35p to 1.6p.

Legislation

[10] The relevant parts of regulation 11 of the 2020 Regulations are as follows:

"**11.**—(1) A registered producer must—…

(e) within the time limits specified in the producer's operational plan, collect scheme packaging first made available by that producer to be marketed, offered for sale or sold for the purposes of its retail sale in Scotland from any of the following—

(i) a return point operator,…

(f) within the time limits specified in the producer's operational plan, pay to a person from whom the producer has collected scheme packaging in accordance with sub-paragraph (e) a sum equal to the deposit for each item of scheme packaging collected,

(g) within the time limits specified in the producer's operational plan, pay to the person from whom the producer has collected scheme packaging in accordance with sub-paragraph (e) a reasonable handling fee charged by that person for each item of scheme packaging collected,…

(3) The obligations in paragraph (1) must be discharged—

(a) where the producer is registered in accordance with regulation 7(1)(a), by the producer, or

(b) where the producer is registered through a scheme administrator, by that scheme administrator, in accordance with regulation 16(1)(a).

(4) For the purposes of this regulation—

a "reasonable handling fee" is—

(a) a fee charged by a return point operator in relation to scheme packaging returned by a consumer to that return point that takes into account the following—

(i) the costs of purchase, lease, maintenance and upkeep of any reverse vending machine associated with the collection and storage of scheme packaging,

(ii) the cost of materials used in respect of the collection and storage of scheme packaging,

(iii) the rental value of any floor space utilised solely for the collection and storage of scheme packaging, and

(iv) staff time dedicated solely to the collection and storage of scheme packaging,"

Submissions for the petitioner

[11] The petitioner's challenge to the respondent's determination of the RHF is a simple one. The petitioner contends that the 2020 Regulations do not give the respondent power to determine the RHF and, even if the respondent had such a power, the RHF has to be based on the costs of the individual RPO as opposed to costs incurred across all retailers operating return points. The petitioner's contention is based upon what was submitted to be a proper interpretation of regulation 11(4). It was further argued that the respondent's approach was contrary to general principles of EU law and, in particular the principles of proportionality, equal treatment and unrestricted competition. In that regard, it was submitted that the RHF set by the respondent was unfair to small enterprises. The petitioner referred to projections which indicated that it would lose approximately £1,000 a week from operating a return point at its store. This, it was submitted, would amount to a distortion of competition between small and large retail enterprises.

Submissions for the respondent

[12] The Answers and Notes of Argument lodged on behalf of the respondent set out how the RHF came to be determined in May 2022. It was explained that the DRS was intended to be an industry-led scheme. The 2020 Regulations set out the basic framework for the scheme with the detail to be determined by the participants in the scheme. It had always been envisaged that the DRS would be developed through a number of contracts including the Membership Agreement and agreements to be entered into between the respondent and individual RPOs. The Membership Agreement provided in general principle 22 and rule 4.14 that an independent entity would be appointed to calculate the RHF. By appointing an independent entity to determine the RHF, it was hoped that this

would avoid some of the difficulties which had arisen in deposit return schemes operated in other countries. PwC had been appointed as the independent entity. PwC had drawn on data from a wide range of RPOs in Scotland as well as from other similar deposit return schemes in operation throughout the world. PwC had followed the terms of the 2020 Regulations in calculating the RHF. By adopting a tiered approach in relation to automated collections, the RHFs calculated were anticipated to be close to cost-neutral for most RPOs and would not disadvantage small enterprises.

[13] It was only at the substantive hearing that the respondent's exact position became clear to the court in relation to the status of the RHF determination issued by it. It was accepted that the respondent had no statutory power to determine the RHF. Nor was it contended that there was any contractual obligation by virtue of the Membership Agreement requiring the petitioner to accept the RHF being put forward by the respondent. It was submitted that the 2020 Regulations were silent as to who was to calculate the RHF. The respondent had stepped into that gap and had appointed PwC to determine the appropriate RHF. The pinch point, according to senior counsel for the respondent, would be when individual RPOs are presented with a proposed agreement from the respondent which will include the RHF rates previously announced. It will be at that point for the individual RPO to sign the agreement or refuse to sign. It was accepted that the respondent could not impose the announced RHF upon the petitioner. In relation to the interpretation of the RHF definition, it was submitted that the factors listed at regulation 11(4)(a)(i)-(iv) refer to general costs experienced by retailers in Scotland as a whole as opposed to individual costs of the specific retailer's return point. It was said that the reference to the fee being charged by the RPO was neutral since payments may be said to be charged by one party even when determined by another. The example of VAT was given.

Decision

[14] As noted in the preceding paragraph, it is accepted by the respondent that it has no statutory power to set the RHF for any RPO. It is also accepted that the petitioner is not contractually bound to accept the RHF announced by the respondent. The first issue for decision, namely whether the 2020 Regulations permit the respondent to impose the RHF upon the petitioner, falls to be determined in favour of the petitioner.

[15] It was not submitted by either party that the Climate Change (Scotland) Act 2009 assisted in the construction of the definition of the RHF in regulation 11(4). The only provision within the 2009 Act which touches upon the RHF paid to retailers is in section 84(7)(d) which provides that regulations made under the Act may include provision about:

> "(d) the inclusion, in the sale price of articles, of a non-returnable element to cover the reasonable costs incurred by retailers, producers or a scheme administrator in administering such schemes".

The 2020 Regulations have not adopted that potential approach of including a non-returnable element in the sale price to cover, *inter alia*, the retailers' handling costs.

[16] I have concluded that the petitioner's construction of regulation 11(4) is the correct one and that the four listed factors which must be taken into account in setting the RHF are by reference to the specific costs of that return point.

[17] The fee is charged by the RPO and it makes sense for the party charging the fee to fix that fee by reference to its own cost base which it will be familiar with. Or, to put it another way, it would be unusual for an RPO to determine the fee charged by reference to costs incurred by other rival RPOs which is information that it will not have access to. Although the respondent argued that the person making the charge does not need to be the person fixing the level of that charge and that is no doubt correct in some situations, the normal

expectation is that a party charging for a service will determine the level of that charge by reference to its own cost base.

[18] Regulation 11(4) also provides that the fee charged is in relation to scheme packaging returned to "that return point" which indicates that the same RPO operating a number of return points may charge a different RHF depending on the costs incurred in operating a different return point. If the respondent's argument was correct, there would be no need to differentiate between return points and this phrase could have been omitted from the regulation.

[19] The factors listed at regulation 11(4)(a)(i)-(iv) are intimately linked to the manner in which an individual RPO will collect and process the scheme packaging at "that return point". There will be differences between operators as to the extent to which staff will be used or whether the process will be mechanised. The extent of floor space in exclusive use for the collection and storage of scheme packaging will vary considerably between return points, as will the rental value of each square foot of floor space. Staff costs and retail floor space must be "solely" related to the collection and storage of the returned packaging in order to be relevant for the RHF assessment. The wording in these sub-paragraphs directs attention to the manner in which the individual RPO operates.

[20] The structure of the 2020 Regulations is more consistent with the petitioner's construction than the respondent's. The 2020 Regulations envisage a scheme administrator being appointed to fulfil the obligations of producers but it is common ground that the scheme administrator has no statutory power in relation to the determination of the RHF. If the regulations had conferred such a power on the scheme administrator then it might have been easier to envisage that an industry-wide analysis of costs was required since a scheme administrator would have an incentive as well as the resources to approach costs on that

basis. By not conferring such a power on the scheme administrator, the clear inference is that individual RPOs should look to their own costs to determine the RHF which they will charge.

[21] Throughout the background papers lodged by both parties there are references to the aim of cost-neutrality in relation to the RHF. In other words, the RPO should neither profit by nor lose by collecting and storing the returned packaging. The only qualification on this aim is that the handling fee be "reasonable" so costs unreasonably incurred by an RPO are not made good. If regard is had to the costs incurred by the individual RPO as opposed to industry-wide costs, the aim of cost-neutrality for each RPO is further promoted.

[22] I have been confirmed in this construction of regulation 11(4) by the terms of the Accompanying Statement to the 2020 Regulations issued by the Scottish Government. At paragraph 109 of that document, the Scottish Government's response to the drafting of regulation 11 stated:

> "We are clear that participation in DRS should be cost-neutral for return points and are broadly satisfied that regulation 11 achieves this. We continue to believe it is appropriate to vary handling fees to reflect different return-point operating models and their associated costs."

[23] I should add that I did not find the parties' submissions in relation to EU principles of any great assistance in construing regulation 11(4). I am unwilling to accept on the basis of the limited documentary evidence available at the substantive hearing that the respondent's approach which includes a tiered system is inherently unfair to small retailers as a group when compared with larger retailers as a group. I also agree with senior counsel for the respondent that if there is a competition law issue linked to the level of the RHF then there is a more appropriate forum for such issues to be resolved. The Competition Appeal Tribunal is far better equipped to analyse the economic data necessary to demonstrate a

detrimental effect on competition. Further, in relation to the principle of proportionality, for reasons discussed in the following paragraphs, I am not convinced that the respondent's approach is in clear breach of that principle.

[24] In advance of the substantive hearing, the respondent lodged an affidavit from Donald McCalman, the respondent's programme director. Reference was made to that affidavit to demonstrate that the respondent's approach to the issue of the RHF had fully complied with EU principles of proportionality, equal treatment and good administration. For reasons briefly set out at para [23], I did not find the submissions on EU law of any real assistance in relation to the interpretation of the 2020 Regulations. However, one paragraph of the affidavit is worth noting in relation to the approach to regulation 11(4). The paragraph sets out the respondent's view on the practical difficulties which would arise if, as I have concluded, regulation 11(4) falls to be construed as the petitioner submitted:

> "41. From a practical perspective, if individual RPOs set their own RHF this would require a substantial additional investment in CSL systems and resources to review and engage with as many as 25,000 individual businesses and to make significant changes to IT systems to allocate specific fees to each company. This investment would be permanent to accommodate annual reviews and other changes. The cost impact would feed directly onto the price of drinks in Scotland and so directly impact consumers."

[25] It is easy to understand the concern expressed by Mr McCalman where a scheme administrator is faced with individual RPOs setting their own RHF by reference to their individual costs. This might also be a concern to some individual RPOs. While the DRS is in its infancy, an individual RPO will have limited information on the costs involved in operating their return point. The amount of scheme packaging to be returned via each return point is unknown. The absence of any bespoke dispute mechanism within the 2020 Regulations means that any dispute between an individual RPO and the respondent as to that RPO's reasonable costs would require to be resolved in court proceedings. This is

likely to be an expensive and time-consuming process for an individual RPO involving the engagement of accountancy and economic experts. These considerations might cause some RPOs to favour an industry-wide RHF provided that the RHF arrived at was close to their own anticipated costs. However, the difficulty for the respondent is that it must operate within the terms of the regulations as enacted. If the practical implementation of regulation 11(4) was thought to be impractical or excessively costly then the solution for the respondent was to ask the Scottish Government to reconsider the terms of that regulation. What the respondent has sought to do is to adopt an approach which may have some practical benefits to commend it, but which ignores the clear wording of regulation 11(4). The petitioner is entitled to insist that the setting of the RHF fee for its return point follows the approach set out in the regulations.

[26] I wish to make clear that although I have concluded that the respondent's approach to regulation 11(4) was in error, it does not necessarily follow that the RHFs calculated by PwC are of no value. On the reasonable assumption that the data used by PwC is broadly based and has been appropriately analysed, the RHF levels proposed by the respondent may be close enough approximations for many RPOs. Individual RPOs might be happy to accept the RHF figure put to them by the respondent as being a close approximation to their costs. For some RPOs, the RHF on offer may be attractive and acceptable simply to avoid the difficulty of isolating and analysing the costs associated with their own return points on an annual basis. But on the basis of regulation 11(4), individual RPOs can insist that the RHF which they charge is to be calculated by reference to their own reasonable costs in collecting and storing the scheme packaging.

Disposal

[27] As suggested by parties, I shall have the case put out by order to discuss the disposal of pleas-in-law and the terms of any declarator. The issue of expenses is reserved meantime.