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Graft, the Mob and the Coming Cartel

The New Administration's Trash Plans for New York City Hold Promise, But Need Expansion to Restore Competition

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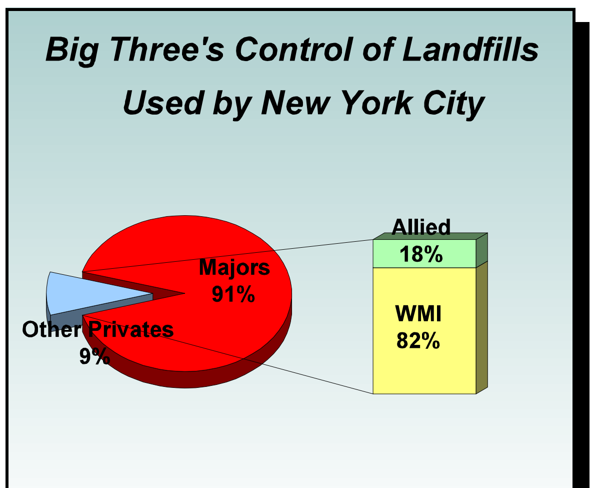
Over the past 125 years, New York City's history for handling its mountain of garbage has gone through three epochal chapters. In the first, it had been mottled by graft, then it suffered extortion by the mafia, and, when last seen, was about to be unceremoniously thrown into the maw of the emerging cartel ...when, suddenly, a ray of sunshine emerged.

New York's new mayor, Michael Bloomberg, was left to pick up the pieces bequeathed him by his predecessor. Former Mayor Rudolph Giuliani's plans to privatize disposal – by contracting with Allied Waste to containerize New York's waste in Linden, New Jersey for rail haul to far-away sites – had crash landed amidst New Jersey politics. This past August, Bloomberg finally began to get the City's act together with the beginnings of a sensible plan for handling its residential trash – *but only if the City keeps control of negotiations and the plan is expanded to also serve the commercial sector.*

Bloomberg was handcuffed by Giuliani's precipitous 1996 deal to close Fresh Kills landfill, the only City disposal site, by the day after he left office in 2001 – even though the site had 20 years remaining life and no replacement plan had been developed.



SOURCE: Chartwell Information of area landfills >1,000 tpd

But, the new administration was not bound to Giuliani's inexplicable attempt to next privatize disposal to Waste Management, Allied and IESI, by giving them control over aggregating and long-hauling New York's trash to distant landfills. After all, the City should have learned a lesson from the debacle it created in 1956 privatizing commercial hauling. That had led to a reign of terror by the mafia that, until busted up by prosecutors in 1995, cost New York's 250,000 commercial businesses billions of dollars as the mob's tax.

None of those vertically-integrated national firms are the White Knights to benignly replace the mafia as Giuliani envisioned. For, as the mob is being moved out, these companies are moving in, spider like across a chess board, to lock down control over almost every yard of landfill capacity accessible to the region and not nailed down in public ownership. Since landfills, with their high barriers to entry, act as a bottleneck in the garbage business, Giuliani's vision would have jumped from the frying pan into the fire.

So certainly, it is true that the City does not need any more stories like the one reported in the June 9, 1996 *New York Times*, about Salvatore Benedetto, a paper recycler who attempted to break into the closed New York trash market where customers had been the mob's property right. After "two men set fire to an empty truck," Mr. Benedetto walked up to a restaurant to meet with the mob to discuss terms but only succeeded in getting "punched in the stomach and choked. ... 'You'll have a lot more problems down the road,'" he was warned, "'if you don't return my customer.'" When, undeterred, Mr. Benedetto continued wooing customers away from the mob, "two men emerged...with a baseball bat and attacked a driver. ... 'We ain't giving people no breaks,'" a solider in the Genovese family later bragged to other cartel members, "'we ain't going to let the customers get off the hook. No. It don't happen.'"

And, sure it is also true that the CEOs of national waste firms who Giuliani lured in to replace the mob may wear pin strip suits instead of wielding base ball bats. But, as subsequent experience showed, inflated prices for waste services from mega-mergers, collusion, price squeezes, predation and undue political influence actually have the potential to take more of a hit out of the economy of New York than those enforced by arson, severed dog heads and crow bars.

Examine the record compiled by oligopolies. The 1980's *Cumberland Farms* class action antitrust lawsuit exposed the waste giants' secret meetings of the "Splinter Group of the New York Society" at which Waste Management's (WMI) Donald Flynn met with Browning Ferris' (BFI) George Farris to signal the next year's price increases.

WMI salespersons like Sandra Blackman would quickly pick up what was going on when they mistakenly tried to win business and make commissions by taking away a customer from a competitor who was a member of the cartel. Ms. Blackman told attorneys for the plaintiffs how she asked her manager for a bid price to compete against BFI for a big customer which was being handed a 35% price increase. "I was told to double — double the 35%. It was almost laughable to call people back," she later testified.

Or, up in Vermont where a jury became enraged and awarded $6 million in damages when it heard that a BFI district manager had told his salesman to threaten Kelco Disposal, a competing independent hauler –

> "If you have to drop your prices, drop your prices and croak him, put him under ... put him out of business. Do whatever it takes. Squish him like a bug."

Antitrust prosecutors have never had the resources to do anymore than temporarily slow down the waste industry's collusive habits – settling those cases that they did bring for chump change and other half hearted divestitures of overlapping assets. They knew things like evergreen contracts were competition killers, but when the consolidators dug their feet in resisting their abolition in settlement talks, prosecutors were not willing to commit the resources to prosecute in order to stop the practice.

But, direct collusion became too easy to be discovered and too counterproductive to be continued. There were too many people “in the know” to keep the facts from the plaintiffs’ bar lured by the prospect of treble damage suits that are available in antitrust cases and were very costly for the consolidators to settle. Then, too, withering public exposure from these messy cases impaired the waste giants’ access to the white shoe capital markets.

More recent and relevant to the future risks of monopoly rents for carting faced by New York City’s commercial sector is the Eastern Environmental story. That tale shows how the large waste consolidators act today and may be expected to proceed tomorrow to stifle competition in commercial carting.

In order to take over the major competition in the Northeast without attracting the Justice Department’s unwanted attention, USA Waste and Waste Management used a stalking horse stratagem. First, Don Moorehead, USA Waste’s prior CEO, installed the once-legendary John Drury as his successor. Next, he brought along his brother, George’s Cayman Islands off-shore private investment pool, Environmental Opportunities Fund, to capitalize the scheme.

Then, they quietly took over Eastern Environmental, which at the time was just a bit player in the market with less than $8 million in annual revenues. From the USA Waste stable, they installed their stalking horse, Lou Paolino, as Eastern’s new CEO. Eastern was infused with cash to acquire a retinue of local and regional haulers that brought Eastern’s run rate in less than two years to more than $170 million. At that point USA Waste, which had taken over Waste Management along the way, merged with Eastern, all according to their prearranged plan.

Now, came the time for payoff. Before the ink was dry on the Justice Department’s acquiesce to the Eastern merger, the March 1, 1999 *Waste News* reported that WMI had instituted tipping fee increases ranging from an “eyepopping” 40% to 138%, in the Northeast, for an unweighted average of 89%.

Although it later turned out the WMI was premature in its estimation of how much of their competition had been eliminated by the merger, the short-lived price hikes graphically illustrated the magnitude of increases it may be expected to impose once the consolidators finally do achieve market power. That oligopoly-tax by the corporate suites would have worked out to about 60% on the total cost to haul away commercial trash in New York, which is substantially more than the 40%-50% levy that Rand estimated to have been imposed by the mob.

None of this, incidently, is a fanciful conspiracy theory. We know all about what actually went down in the back rooms because, after Mr. Drury was, in turn, forced out as CEO of Waste Management in the wake of another accounting meltdown in 1999, the next bull pen to fill the company’s executive suite revealed the facts of the conspiracy when it sued its predecessors in the case, *Waste Management v. Paolino*. Apparently, through self-dealing in many of these transactions, they had stolen tens of millions of dollars for personal enrichment along the way as they built a foundation aimed at establishing a Northeast cartel.

All this history bears directly on the City’s marine station proposal because, as noted, disposal is a bottleneck, and environmental regulations along with fierce local opposition to either landfills or transfer stations have created enormous barriers to entry into disposal markets. Bottlenecks and barriers to entry are a prescription for monopolization. In New York City, because there are no nearby landfills following the closure of Fresh Kills, the operative facility for market power has become the transfer stations that are take off points needed to long haul to faraway disposal sites.

Until Allied's Linden proposal aborted, WMI, Allied and IESI seemed poised to eliminate the ability of the independent carters to compete effectively by dominating the private land transfer stations in the City. If the consolidators controlled most of them, they could charge competitors more than they price the service for themselves, and, thereby, make it impossible for independents to compete. With control over transfer stations, price squeezes could be exploited to enforce cartel pricing against independents.

Fortunately, instead of contracting out disposal of the City's trash, New York's new Mayor is now prudently preparing to refurbish its existing network of marine transfer stations (MTS) – once used to barge trash to Staten Island – in order to prepare the residential trash for shipping to remote landfills.

What's missing from these new plans, however, are two things. First, the City still has not committed to, itself, containerizing the loads at a central site and setting up a new marketing authority to directly negotiate laddered deals for disposal. Instead, it may slide back to contracting with two or three private firms that guarantee to take the City's waste for the next 20 years. The problem with such a hand-off approach is the only companies which can do that are the waste giants who are positioning themselves to impose monopoly rents.

Second, the City is ignoring the enormous benefits from expanding a residential marine transfer strategy to the commercial sector, coupled with a phase out of land-based transfer stations. For, until the marine transfer station proposal emerged, the Big Three appeared poised to eliminate the ability of the independent carters to compete by using their control over private transfer stations to price squeeze the little guys. By expanding the new proposal to adapt the marine transfer stations for commercial along with residential flows, a relief valve would be created to protect the independents from price squeezes.

In view of the Department of Sanitation's lack of interest to date, expansion will depend on whether those most at risk from the loss of competitive markets — from the Hilton Hotel to Sid's Pastrami Shop — demand protection. Sure that would make the City's work more complicated. But, every penny extracted by an illegal monopoly tax for waste services subtracts from households' and businesses' ability to pay the lawful property taxes the City so desperately needs. ❐