

MEETING:	CABINET
DATE:	16 FEBRUARY 2012
TITLE OF REPORT:	WASTE CONTRACT – VARIATION
PORTFOLIO AREA:	MAJOR CONTRACTS

CLASSIFICATION: Open

Wards Affected

County-wide

Purpose

To authorise the parameters of negotiations with our contractors concerning the variation to the integrated waste contract and to note progress to date in those negotiations.

Key Decision

This is not a Key Decision.

This item was originally included in the Forward Plan in the expectation that it would require a decision on expenditure over £500,000. In the event, no financial decision is to be made at this stage and a further report to Cabinet will be required in due course.

Recommendation(s)

THAT:

- (a) Cabinet notes progress since the reports to Cabinet in September 2009 and January 2010;**
- (b) subject to recommendation (d) below the Director for Places and Communities be authorised, in consultation with the Chief Officer Finance and Commercial and Worcestershire County Council, to agree the negotiated form of a variation to the existing waste contract with Mercia Waste Management Ltd (Mercia) to put into effect Mercia's proposals for:
 - i) the provision of a residual waste treatment facility (RWTF) using Energy from Waste technology at Hartlebury Trading Estate; and**
 - ii) such other ancillary issues as are appropriate in relation to the waste contract (collectively 'the contractor's proposals') provided****

Further information on the subject of this report is available from Andy Tector,
Head of Special Projects on (01432) 261989

such a variation is in compliance with

- a) the planning parameters**
- b) the financial parameters**
- c) the contractual parameters and**
- d) the technical parameters.**

(all are set out in this report and collectively the 'parameters'); and

- (c) the Director for Places and Communities provides a further report to Cabinet seeking formal authority to execute such a variation when he considers, having regard to any advice from the appointed advisors, that the parameters have been materially satisfied; and**
- (d) the authorisation under (b) is subject to Worcestershire County Council giving approvals substantially in the same form as those contained in the recommendations of this report and the two councils agreeing in principle to extend the joint working agreement in so far as it relates to the Energy from Waste facility for a period commensurate with the intended life of the facility.**

Key Points Summary

- The report outlines the progress to date on the negotiations between the two councils and Mercia.
- The report outlines parameters around which future negotiations should be based to bring forward a variation which would put into effect Mercia's proposals for a residual waste facility and any ancillary issues in relation to the waste contract.
- The report also provides an in principle agreement to extend the joint working agreement between the two authorities in so far as it relates to the Energy from Waste facility at Hartlebury for a period commensurate with the intended life of the facility.

Alternative Options

- 1 At this stage there are no alternative options to consider and the recommendations will require further ratification by Cabinet at the conclusion of the negotiations.

Reasons for Recommendations

- 2 The recommendations give officers authorisation to continue negotiations with Mercia within the context of the parameters in Appendices 1 – 5.

Introduction and Background

- 3 This report refers to the Waste Management Private Finance Initiative (PFI) Contract (the 'waste contract') that was entered into between Worcestershire County Council and Herefordshire Council (the councils) and Mercia Waste Management Ltd in December 1998. The two councils act jointly as waste disposal authorities and any variation to the waste contract would need to be agreed by both councils.

4 At the Cabinet meeting of 7 January 2010 the then Director of Environment and Culture set out the recent history of the waste contract, and some of the key terms and the statutory targets that have been set for waste disposal authorities for the diversion of biodegradable municipal waste from landfill. The Director of Environment and Culture was authorised to encourage Mercia to bring forward proposals under the existing PFI contract for future residual waste treatment and to negotiate with Mercia with a new to a potential variation to give effect to the EfW proposal.

5 On 10 September 2009, the Director of Environment and Culture presented a report on the first review of the Joint Municipal Waste Management Strategy (JMWMS) which Cabinet endorsed and adopted. Paragraph 20 of that report contained the following text:

*20. The prescriptive approach to treatment of residual waste by an autoclave process has been removed in the revised strategy. There is now a new policy to increase diversion away from landfill supported by a Residual Options Appraisal (Annex D). * This provides a detailed appraisal for waste treatment options capable of increasing the value derived from the residual waste stream. The appraisal informs the method for future treatment of residual waste, proposals for which are expected to come forward from the Waste Disposal Contractor (Severn Waste Services). The robustness of the strategy is important in supporting necessary applications for planning consent.*

(*included in Appendix 5)

6 On 10 November 2009, Mercia presented a project proposal to the councils for the construction of an Energy from Waste Plant at Hartlebury (the EfW Proposal).

7 Entec, specialist technical advisers to the councils on waste, had examined the EfW proposal both in relation to their own assessment of the councils' requirements and the JMWMS. The executive summary of Entec's report concluded that the EfW Proposal was compliant with the JMWMS and would meet the councils' needs.

8 On 7 January 2010 Cabinet resolved that, subject to similar approvals having been given by Worcestershire Council and having due regard to the technical assessment received from the technical advisers to the councils in relation to the EfW Proposal described in paragraph 6 of the report, and the Joint Municipal Waste Management Strategy:

- a) the concept contained in the EfW proposal and the progression of the proposal to the planning stage be supported in principle;
- b) the Director of Environment and Culture be authorised, in consultation with the Director of Resources and the Assistant Chief Executive (Legal and Democratic), to enter into negotiations with Mercia and to prepare a potential variation (the variation) to the waste contract to give effect to the EfW Proposal for subsequent consideration by Cabinet should planning permission be granted in respect of it;
- c) the land at Hartlebury Trading Estate already within Worcestershire County Council's ownership was appropriated for the planning purposes of the EfW proposal;
- d) a further report be received in due course to consider any potential variation to the waste contract.

9 This report is now brought to Cabinet in line with paragraph 8(d). The post of Director of Environment and Culture has subsequently been superseded for these purposes by the Director for Places and Communities. The post of Director of Resources has been

superseded by the Chief Officer – Finance and Commercial, and the post of Assistant Chief Executive (Legal and Democratic) has been superseded by the Assistant Director – Law, Governance and Resilience.

- 10 Mercia subsequently made an application for planning permission for the EfW proposal which has been the subject of a recent planning inquiry. Such an application would be dealt with by Worcestershire county Council as the relevant planning authority. Worcestershire County Council's Planning and Regulatory Committee was minded to grant consent but the matter was called-in by the Secretary of State. A public inquiry was held by an inspector in November 2011 and the Secretary of State's decision is due on or before the 23 April 2012.
- 11 In the event that the Secretary of State grants planning permission for the EfW proposal, and contractor's proposals are acceptable, the councils acting jointly need to be in a position to be able to effect a suitable variation to the waste contract.

Key Considerations

- 12 The recommendations as detailed above and the parameters outlined below provide the scope within which the negotiations, to conclude the variation to the waste contract, should be conducted. A further report will be presented to Cabinet at the conclusion of the negotiations.
- 13 Parameters – generally
Given that the waste contract is already in effect pursuant to the decisions of the councils at its inception and subsequently (in relation to any changes), and in order to avoid iterative decision-making on points of detail which are likely to be meaningless in isolation, it is suggested that Cabinet defines a mandate by reference to certain parameters ("the parameters") within which any variation can be concluded.
- 14 Planning Parameters
Without an effective planning consent, Mercia will be unable to bring forward their contractor's proposals. Notwithstanding this point, the councils may not be prepared to accept contractor's proposals based upon any planning consent e.g. where conditions on hours of operation or sources of waste collection render the plant vulnerable to becoming uneconomical, particularly beyond expiry of the waste contract. The councils' position on these issues is defined at Appendix 1 – Planning Parameters.
- 15 Financial Parameters
In deciding whether or not to approve the recommendations contained in this report, Cabinet will no doubt want to know that any variation would:
 - (a) be affordable;
 - (b) represent value for money; and
 - (c) not burden the councils with unpredictable costs in the future.
- 16 The waste contract already contains a payment mechanism which applies a baseline fee for each tonne of waste received by Mercia, with an uplift fee per tonne for treatments other than landfilling such as recycling, energy from waste (EfW) etc. Consequently, the price effect of variation will manifest itself as a change to the payment mechanism, particularly the EfW uplift, derived from a complex financial model. The model is sensitive to many inputs such as tender costs, interest rates, foreign exchange rates, in so far as equipment is purchased outside the UK, swap rates and other financial data sets. Whilst the EfW uplift may be the focal point of intensive, commercial negotiations, it is suggested that it is not an appropriate defining parameter due to:
 - (a) the volatility and transient nature of some of those inputs, particularly in current markets;

and

- (b) the absence of reliable comparators due to the split between the baseline Fee and the EfW uplift.

17 When Cabinet receives a further report on a proposed variation it will no doubt consider the overall cost envelope in the context of current budgets plus projections and the projected cost of doing nothing or the cost of starting the procurement process afresh.

18 The financial parameters set out in Appendix 2 are intended to address all of the points referred to in the paragraphs above.

19 It should be noted that, based on Mercia's proposal, the councils would be obliged to make a "balloon payment" upon termination or expiry of the project agreement. The amount of balloon payment due at any point in time will relate to the amount of bank funding outstanding in relation to the EfW at that time and is therefore expected to be set out in the variation.

20 Contractual Parameters

Legally enforceable public procurement rules have been established to prevent public bodies from improperly purporting to use variations to existing contracts to avoid costly and time-consuming re-procurement. Two golden rules are that:

- (a) there must be no material change in the services and means of delivery compared with that envisaged when the original contract was let; and
- (b) if there is any change in the risk/reward share in the original contract, it should not be to the benefit of the contractor.

21 In relation to the former point, aside a refresh of the Energy from Waste technology:

- (a) particularly in relation to pollution control, the services and means of delivery to be procured in the EfW proposals are essentially the same as the original proposal but in a different place at a different time with a similar capacity adjusted to reflect updated waste flow predictions.
- (b) In relation to the latter point any amendments to the contract will be limited to those necessary to give effect to the contractor's proposals and to any benefits the councils are seeking from the opportunity created by the making of the variation. The councils' position on these issues is defined in Appendix 3 – Contractual Parameters. Importantly the intention is that Mercia's rate of return is not improved.

22 Technical Parameters

The original intention of the waste contract was that the EfW plant life would be commensurate with the duration of the contract period and so handback condition was of little concern; any remaining useable life (for which see, for example, Coventry) would have been a bonus. The variation proposes the return of the facility to the councils with more than half of its economic life left to run (together with the outstanding debt to which the balloon payment relates) and so the hand-back condition, together with anticipated life cycle costs and accrued maintenance reserves become critical; the councils' position is defined in Appendix 4 – Technical Parameters. Accordingly, it will be important for the two councils to agree in principle to extend the joint working agreement insofar as it relates to this EfW facility for a period a commensurate with the intended life of the EfW facility.

23 Appointed Advisors Opinion

Recognising that Cabinet and officers will properly be relying on the advice of the councils' advisors dealing with legal, technical and financial issues (the appointed advisors) who hold the requisite professional indemnity insurances in relation to the advice they give to the councils, it is suggested that any future delegated mandate to execute the variation be subject

to receipt of appropriate advice from the appointed advisors recording their opinion in relation to the extent to which the parameters have been met.

Community Impact

- 24 As the report mainly refers to the provision of a residual waste treatment facility at Hartlebury in Worcestershire, the impact of this report is minimal. However the current landfill site has a very limited life and there would be impact on the community should an alternative method of residual waste treatment not be developed.

Equality and Human Rights

- 25 The decision would have no impact on our public sector equality duty.

Financial Implications

- 26 Appendix 2, the Financial Parameters outlines the financial scope of the councils' negotiations. The recommendations do not at this stage commit the council to expenditure. However, should the recommendations not be adopted there is potential scope for the contractor to seek to terminate the contract with the council's having to meet their respective proportion of the cost of termination and/or the Department of Environment, Food and Rural Affairs terminating the two councils PFI credit. Herefordshire Council currently receives £1.362 million per annum in PFI credits. This will continue until December 2023.

Legal Implications

- 27 Appendix 3 to the report outlines the contractual parameters for ongoing negotiations and outlines the legal issues that will need to be satisfied before any variation can be concluded.

Risk Management

- 28 The variation of the waste contract is recorded as a risk in the corporate risk register (RSK.PAC.003 PBC 003).
- 29 At this stage the recommendations do not in themselves pose any risk as a further report will need to be made to Cabinet before any variation can be confirmed.
- 30 Should the recommendations not be adopted there is potential scope for the contractor to seek to terminate the contract with the councils having to meet their respective proportion of the cost of termination and/or the Department of Environment, Food and Rural Affairs terminating the two Councils PFI credit.
- 31 It is expected that the councils will be obliged to make any balloon payment (see paragraph 19) to the bank irrespective of the condition of the EfW at the relevant time or any other breaches of the waste contract by Mercia. The councils would therefore have to pursue Mercia for any losses arising (e.g. as a result of the EfW not being in the required condition). There is a risk that at that point Mercia are not good for the money and the councils are left overpaying for a 'broken' plant. This risk may be mitigated and managed by proactive contract management during the term and parent company guarantees from a company of sufficient strength and a bank bond for a sum which the councils expect to be sufficient to cover any overpayment

Consultees

32 Worcestershire County Council

Appendices

Appendix 1 – Planning Parameters

Appendix 2 – Financial Parameters

Appendix 3 – Contractual Parameters

Appendix 4 – Technical Parameters

Appendix 5 – Joint Municipal Waste Management Strategy – Annex D

Background Papers

38 None.