

Waste loan risk register

24.11.15

Appendix d

Risk Reference	Description of risk	Gross Impact	Gross Probability	Gross Risk Score	Risk control approach	Mitigating Actions	Residual Impact	Residual Probability	Residual Risk Score	Assigned to (Risk Owners)
a	Default of loan repayments by borrower to lenders due to SPV (Mercia) or HZI falling into administration.	Critical	Medium	15	Risk transferred	Due to the security package negotiated by the Councils a fall away analysis indicated that Mercia, its Shareholders and HZI would need to enter administration at the same time to put repayment at risk during the construction phase. The maximum exposure to the Councils has been calculated and included within the sufficiency assessment of the Council's reserves. All press articles are scanned regularly for indications of financial strength issues and followed up to ensure counterparty risk is not increased.	Substantial	Very low	6	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default and Deloitte to monitor Mercia's actual quarterly cash flow tests and cover ratios that have to be maintained by Mercia.
b	Construction completion date of EfW is delayed and delays repayment of loan to lenders.	Substantial	Medium	11	Risk transferred	Under the contract terms agreed with Mercia, Mercia take all material risk on EfW construction delay and repayment of loan will commence around February 2017, as set out in the SLFLA and agreed final financial model. Repayments are not tied to the actual construction completion date, rather the planned date. The Council as lender has the right to call the loan into default if construction is not completed by a long stop date, 18 months after the loan repayment date. The lenders technical advisor has confirmed that the expected takeover date is now the planned takeover date plus one month, 31.03.15	Substantial	Very low	6	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.
c	PWLB borrowing rates increase more than estimated in the Councils' prudential borrowing model. Higher rates would reduce the surplus generated on the loan arrangements with Mercia.	Substantial	Low	10	Risk treated	The cost of purchasing a financial product to remove this risk (a swaption) from an investment bank was quoted at £20m. The Councils decided to manage the risk through forecasting the forward price for its debt draw downs over the construction period and hold in reserve monies to mitigate this risk where required. Currently the rates accessible by the Councils are lower than this estimate as the continued low gilt rate environment pervades.	Substantial	Very low	6	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.

d	Loan drawdowns are slower than set out in the STFLA. Delayed drawdowns would result in reduced interest payments to the Councils and potentially reduced surplus if PWLB loan rates increase between the expected draw date and actual.	Negligible	Medium	4	Risk treated	The Councils plan to borrow in line with its Treasury Management Policy. Therefore the Councils would receive reduced interest receipts but less interest would also be payable. The Councils are monitoring market gilt rates actively and have the option to borrow from PWLB up to a year in advance of expected drawdown requests. Regular progress reports are being reviewed to ensure the construction programme and the loan drawdowns are requested in line with the plan.	Negilible	Very low	2	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.
e	Drawdown requests from Mercia are not actioned by the Councils or not actioned within the required contracted time period.	Substantial	Low	10	Risk treated	The Councils treasury teams have been fully briefed on the actions required to fulfil drawdown requests, checks required and the contracted timeline by the Section 151 Officer and their teams. Drawdowns to date have been actioned in line with requirements.	Substantial	Very low	6	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.
f	Mercia loan principal and / or interest repayments are below the required values as per the rates agreed in the STFLA .	Substantial	Very Low	6	Risk treated	The Councils treasury team maintain a spreadsheet detailing drawdowns to date and expected future principal and interest payments. This is reconciled to Mercia's repayment spreadsheet and will be matched to principal and interest repayments received from Mercia during the post construction period.	Substantial	Almost impossible	5	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.
g	Default of repayments by borrower to lenders due to HZI termination of Interserve Construction Limited (ICL) delaying project completion to after long stop date.	Critical	Medium	15	Risk treated	Sponsors have provided assurance that they believe HZI are undertaking the right processes to replace ICL work packages and that there is no financial risk to the Sponsors from the work underway. Sponsors confirmed that their due diligence on HZI had not raised any concerns around the companys viability or going concern. The Councils as lenders have the right to call the the loan into default if construction is not completed by the long stop date, at which point the negotiated security package, set out in section a above, would take effect.	Substantial	Very low	6	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.

h	HZI termination of ICL may weaken the negotiated security package due to no single new supplier exceeding £10m contract value and therefore triggering EPC Contract Schedule 7 requirements for Collateral Warranty and professional indemnity insurance requirements. The risk is that the Council as lender does not receive the same security package as it had when ICL was in place.	Substantial	High	12	Risk treated	In terms of Collateral Warranty, the HZI Collateral Warranty is in place and remains in place. Due diligence has been undertaken by Sponsors and the Councils as lenders (with the Financial Advisor) to confirm the financial strength of HZI in light of events. There are no issues arising from these reviews. Sponsors have agreed to review on a case by case basis the requirement for additional security protections and will advise the Councils as to its rationale for its decision. The Councils as lenders have sign off rights and requests have and will continue to be made to the Councils prospectively for Schedule 7 services and retrospectively (based on Sponsor assurance) for non-Schedule 7 services. Planned meetings have been held and will continue to be arranged for sign off and Council advisors have been retained to provide advice. The Councils have clearly articulated to Sponsors that there should not be any weakening on the Security Package in place with regard to the Civil Engineering Work. There is no financial impact on Sponsors from events to date and therefore no financial	Substantial	Low	10	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.
---	---	-------------	------	----	--------------	--	-------------	-----	----	--

Key		
Score	Risk judgement	
1-7	Low	Acceptable risk: need periodic review, low cost control improvements sought if possible
8-18	Medium	Acceptable risk: close monitoring and cost effective control improvements sought
19-24	High	Unacceptable risk: immediate control / improvement required

Scoring Matrix

Likelihood	Very High	9	19	21	21
	High	8	12	20	23
	Medium	4	11	15	24
	Low	3	10	14	18
	Very Low	2	6	13	17
	Almost impossible	1	5	7	16
		Negligible	Substantial	Critical	Extreme
		Impact			