

Title of report: Energy from waste loan update

Meeting: Audit and Governance Committee

Meeting date: Tuesday 29 October 2024

Report by: Director of Finance, Chief Accountant

Classification

Open

Decision type

This is not an executive decision

Wards affected

(All Wards);

Purpose

To update the committee on the current status of the energy from waste loan arrangement to enable the committee to fulfil its delegated functions.

Recommendation(s)

That:

- a) **The risks to the council, as joint lender, are confirmed as being reasonable and appropriate having regard to the risks typically assumed by long term senior funders to waste projects in the United Kingdom and best banking practice; and**
- b) **Arrangements for the administration of the loan are reviewed and confirmed as satisfactory.**

Alternative options

1. None; the loan arrangement was contractually agreed in May 2014, no breaches or areas of concern have taken place during the reporting period. This report provides an update on the arrangement to the Audit and Governance Committee in its role as the waste loan governance committee which entails reviewing risks to the lender and monitoring administration of the loan.

Key considerations

2. In 1998, the council, in partnership with Worcestershire County Council, entered into a 25 year contract with Mercia Waste Management Limited (Mercia) for the provision of an integrated waste management system using the Private Finance Initiative. In 2014, a variation to the contract was signed, to build, finance and operate an energy from waste plant in Hartlebury.
3. The councils (the Lenders) provided a total of £163.5 million to Mercia (the Borrower) as a long term loan split across two facilities (Facility A £35.45 million and Facility B £128.05 million). Herefordshire Council provided 24.2% of the loan (value £39.57 million).
4. Facility A was fully repaid in December 2022. The repayments for Facility B have been extended for 5 years until January 2029 in line with the extension to the Waste Management Services contract.
5. This report enables the committee to fulfil the functions delegated to it in relation to the governance of the waste loan arrangement; specifically to review the risks to the council as lender and to monitor administration of the loan.
6. Since the last report to the committee in December 2023, the loan arrangement has continued to be repaid in line with expectations, and risks to the council are considered to be reasonable and appropriate.
7. The ownership of Mercia Waste Management has changed. In June 2024, FCC Servicios Medio Ambiente completed the purchase of Urbaser UK (one of the two main owners of Mercia Waste Management). The impact of this on the parent company guarantee and the loan facility is considered in Appendix 3, the joint risk register.

Update to loan balance

8. During the last year, since the previous report to the committee, the following loan repayments have been made:

	Interest £m	Principal £m	Total £m
Loan balance (principal) at December 2023		29.7	
December 2023 repayment	0.9	0.3	1.2
June 2024 repayment	0.9	0.9	1.8
Loan balance (principal) at October 2024		28.5	

Loan Agreement Ratios

9. The ratios are a financial covenant imposed by Lenders (in this case the council and Worcestershire County Council together as Lenders) as a monitoring mechanism to provide early warning of project distress and potential Borrower (in this case Mercia) default on their repayment obligations. The ratios provide a measure of the project's historic and future performance in relation to its ability to service current and upcoming debt liabilities. The ratios are reported every 6 months in June and December.

10. The ratios reported at June 2024 were as follows:

Ratio	Calculation	Reason	Compliance value	Actual value at June 2024	Actual value at June 2023
The Historic Annual Debt Service Cover Ratio	Preceding 12 months actual cash flows Divided by Loan principal and interest repayments over the preceding 12 months	To assess the ability to service current debt obligation over the preceding 12 month period	1.35	2.22	1.58
The projected Annual Debt Service Cover Ratio	Following 12 months actual cash flows Divided by Loan principal and interest repayments over the next 12 months	To assess the ability to service future debt obligations over the following 12 month period	1.35	1.98	2.30
The Loan Life Cover Ratio before distributions	NPV all future cash flows plus available reserve balances Divided by Loan principal outstanding	To assess the ability to repay the outstanding loan balance from future cash flows over the remaining life of the loan	1.40	9.05	7.77

11. The ratio calculations have been supplied by Mercia along with forecasts of future ratio value up until the end of the loan agreement. There are no ratios that are forecast to be below the agreed compliance values.
12. Mercia have supplied a Ratio Compliance Certificate confirming that, as at June 2024, all ratios are within the levels outlines in the Senior Term Loan Facilities Agreement. There are no areas of concern to highlight to the committee. This Certificate is included in Appendix 1.
13. Mercia have supplied a Senior Term Loan Facility Agreement Assurance Statement for Lenders to provide some assurance to the council that loan covenants have been met, and there are no significant issues or risks to future loan repayments. This Statement is included in Appendix 2.

Community impact

14. In accordance with the adopted code of corporate governance, the council must ensure that it has an effective performance management system that facilitates effective and efficient delivery of planned services. Effective financial management, risk management and internal control are important components of this performance management system. The committee's assurance that any risks associated with the loan arrangement have sufficient mitigation actions applied supports adherence to the code.
15. The loan arrangement supports the continued viability and affordability of the contracted waste disposal arrangement.

Environmental Impact

16. Herefordshire Council provides and purchases a wide range of services for the people of Herefordshire. Together with partner organisations in the private, public and voluntary sectors we share a strong commitment to improving our environmental sustainability, achieving carbon neutrality and to protect and enhance Herefordshire's outstanding natural environment.
17. This is an update on an existing loan arrangement and will have minimal environmental impacts. However, consideration has been made to minimise waste and resource use in line with the Council's Environmental Policy, which is managed as part of the overall waste collection and disposal service provision.

Equality duty

18. The Public Sector Equality Duty requires the Council to consider how it can positively contribute to the advancement of equality and good relations, and demonstrate that it is paying 'due regard' in our decision making in the design of policies and in the delivery of services.
19. The mandatory equality impact screening checklist has been completed for this activity and it has been found to have no impact for equality.

Resource implications

20. There are no financial implications arising from the recommendations in this report. The loan arrangement is being repaid as expected, the implications of the agreed loan arrangements are reflected in the council's medium term financial strategy and treasury management strategy as agreed by Council in February 2024.

Legal implications

21. The terms and arrangements for this loan agreement are set out in the senior term loan facilities agreement. There are no specific legal implications arising from this report. The function of the committee is set out in the constitution under 3.5.13. This report relates to functions (a) to review risks as lender and (b) to monitor the administration of the loan.

Risk management

22. Attached at Appendix 3 is the joint risk register with Worcestershire County Council.

Consultees

23. None.

Appendices

Appendix 1 – Ratio Compliance Certificate

Appendix 2 – Senior Term Loan Facility Agreement Assurance Statement for Lenders

Appendix 3 – Joint Risk Register

Background papers

None identified.

Report Reviewers Used for appraising this report:

Governance	Jen Preece	Date 15/10/2024
Finance	Wendy Pickering, Karen Morris, Judith Tranmer	Date 18/10/2024
Legal	Sean O'Connor	Date 18/10/2024
Communications	Luenne Featherstone	Date 10/10/2024
Equality Duty	Harriet Yellin	Date 18/10/2024
Procurement	N/A	
Risk	Jessica Karia	Date 18/10/2024
Approved by	Rachael Sanders	Date 19/10/2024