
Executive Meeting

12 September 2006

Report of the Director of City Strategy

Residual Waste Treatment Procurement

Executive Summary

1. This report requests the authority to submit an Outline Business Case (OBC) to DEFRA for PFI funding in line with the objectives of the Joint Municipal Waste Management Strategy 'Lets talk less rubbish' (JMWMS) as agreed by Full Council on 29 June 2006 and Joint Working Agreement (JWA) with NYCC (as agreed at the Executive on 25 October 2005).
2. The key features of the OBC are: -
 - a) The business case has considered a wide range of options, including a range of residual waste treatment technologies that will achieve the objectives of the JMWMS. However it is recognised that new technologies are developing and the ultimate solution may well not be one of the options considered in the OBC. Following risk assessment of a number of options, a reference project has been identified for the purposes of demonstrating a deliverable cost effective solution. At this stage no decisions have been made or are being recommended in relation to the technology to be employed.
 - b) The reference project covers all Waste Management Services except waste collection; the reference case (for which PFI funding is sought) is residual waste treatment services. The remaining waste services (transfer, recycling, composting and landfill) will be procured separately by NYCC and CYC.
 - c) The procurement process will determine the technology to be procured. The market will be invited to put forward any options that satisfy the JMWMS. At a recently held bidders day, a large number and range of technology providers attended with potential solutions (examples included MBT with inert residue and In-vessel composting). The bidders attending were keen to participate in the procurement.
 - d) In accordance with Treasury Taskforce Guidance, the reference project offers value for money,
 - e) The Councils will face an increasing 'affordability gap' between the current levels of service and the 'reference project' cost. They will commit to finding the additional resources to make the project affordable.

- f) Both Councils' officers are identifying potential suitable sites, and work on planning is to be pursued as soon as possible. From the work done to date it is very unlikely that these will be located within the CYC boundary.
- g) Yorwaste will be requested not to participate in the PFI residual waste treatment contract
- h) Delivery standards for waste collection services will need to be achieved.

Purpose of Report

- 3. To request the authority to submit an Outline Business Case (OBC) to DEFRA to bid for PFI funding to provide the necessary technologies to deal with the increasing problems of waste disposal. The key issues for consideration are discussed below: -
 - i) Procurement strategy
 - ii) Value for money and affordability of the project
 - iii) Sites and planning issues
 - iv) The role of Yorwaste
 - v) Partnership arrangements

Background

- 4. The Council approved its current Waste Strategy in November 2004; this was specific to York. In addition the Council supported the Joint Municipal Waste Management Strategy (JMWMS) in July 2006; this revised JMWMS is a high level strategy with key objectives and targets for the partnership (NYCC, NYCC districts & boroughs and CYC). The strategy focuses on waste minimisation, increased re-use, recycling and diversion from landfill. Central to delivery of the strategy is the need to treat residual waste. The partnership/each Local Authority has specific action plans to deliver their contribution to the strategy.
- 5. City of York Council is working on action plans on minimisation, re-use and recycling. This procurement project will deal with waste only after waste minimisation activities have taken place and re-use and recycling have been maximised. It is assumed that some waste will continue to be put into landfill (ensuring that we don't exceed the landfill allowances allocated).
- 6. As part of its current strategy the Council has agreed to work in partnership with NYCC to deliver the residual waste treatment element of the strategy. It was originally anticipated that this would involve letting a single 'semi-integrated' service contract for recycling, transport and treatment of waste. However, recent changes to the criteria for award of PFI projects has required a review of the procurement strategy which has concluded that services should now be disaggregated, with joint procurement limited to treatment of residual waste only. Both Councils have signed a joint working agreement setting out how the Councils' will work together, share responsibilities and costs (Executive 25 October 2005).

7. DEFRA have indicated that some £65m of PFI credits are available subject to Treasury approval of the scheme.
8. This report considers the Business Plan for the waste treatment part of the strategy in the form of an Outline Business Case (OBC). The capital investment needed to deliver the strategy requires a commitment to long-term finance and service provision. The Business Plan proposes a request for PFI funding in support of the project on the basis that PFI provides the only available source of external revenue support at this time. The latest draft Executive Summary is attached at Appendix 1, the key issues are set out below. A copy of the non-confidential parts of the OBC will be made available on request.

Procurement Strategy

9. (1) Scope of the contract

The two Councils, NYCC and CYC, had been considering a semi-integrated approach to waste treatment (i.e. a single long term contract for all waste management services except waste collection). DEFRA will now only support PFI projects focussing on residual waste treatment services. Evaluation work on packaging options and funding approaches was carried out by the Officer Project Group and its financial and technical advisors with support from the Strategic Project Board comprising NYCC and CYC Chief Executives' and Operational and Financial Directors. This concluded that a disaggregated approach offers Best Value with a) the residual waste treatment services and facilities procured through PFI and b) waste handling, recycling and composting services procured using internal resources separately; packaged as each Council believes appropriate. The Councils are therefore seeking PFI credits to support only the residual waste treatment services contract.

One of the major issues in adopting a disaggregated approach (which will mean that the overall delivery is covered by a number of different contracts) is the potential increased number of interfaces between contractors. However it is felt that the disaggregated approach will attract more market interest, and thus competition, which should reduce bid prices. In addition the Government has indicated they will only provide PFI support for disaggregated waste contracts. Significant market interest, for this form of contract packaging from a wide range of differing technology providers, was shown at a recent soft market-testing (bidders) day held in York on 26 July.

- (2) Options Appraisal

There are a range of technology options that could deliver the waste treatment project, taking into account waste strategy objectives, the results of the Best Practical Environmental Option (BPEO) analysis and the results of public consultation. The Councils proposed approach to procurement is to use the Public Private Partnerships Programme (4Ps) model documentation including an output specification, payment mechanism and project agreement.

The output specification enables bidders to put forward a range of proposals that will deliver the objectives of the waste strategy. This means that the Councils will not be determining the technology used but will be specifying through the evaluation criteria how the service will be delivered. The Councils recognise that the eventual choice of technology will be in response to market proposals on how to deliver output targets, and that no one option is more or less likely to deliver a particular technology.

It is therefore important that evaluation criteria are weighted appropriately to ensure the selected bid achieves the objectives of the project. Examples of criteria will be the cost (and therefore affordability) and the environmental impact of the final proposal chosen.

For the purposes of considering the value for money, affordability and delivery of the project it is necessary to identify and cost specific options. Detailed options appraisal work was undertaken to identify a 'reference project' that delivered the objectives identified using evidence from BPEO, public consultation, costings and risk assessments. A summary of this work and conclusions is set out in the Executive Summary.

The **reference project** identified consists of

- Treatment of residual waste (the reference case)
- Transfer and recycling services
- Composting services
- Landfill disposal services

The **reference case**, for the purposes of Outline Business Case (OBC) is: -

- 1 (Mechanical Biological treatment plant) MBT from 2010 in York area.
- 1 (Energy from waste plant) EFW from 2013 in County Council area.
- SRF (Solid Residual Fuel) from the MBT plant, sent to EFW to produce energy.
- In the years between 2010 and 2013 until the EFW is built, it is assumed the SRF will go to landfill.

The 'reference project' has been compared to the 'status quo' situation to ensure the project offers value for money, and to budget projections to check the affordability of the project. This will be considered later in the report.

As explained above, the procurement process will determine the final solution, which may reflect the reference case, but may reflect technologies still developing at this time.

(3) Funding Options

In addition to looking at technology options, risk assessments were undertaken in relation to funding opportunities. Private Funding (PFI), Public Private Partnerships (PPP) and prudential borrowing were all considered as options for the reference project. It was felt that the net impact of receiving additional PFI grant funding outweighed the additional procurement requirements and costs for the residual waste treatment services contract, because of the significant capital investment required. In addition a complex procurement involves significant risks and a PFI or PPP approach enables the transfer of those risks to the private sector. Early soft market testing with potential funders on 25 July 2006 gave a positive response to the proposed procurement methodology.

Timescales

10. The key dates in the procurement timetable as set out at table 1.8 in the Executive Summary, are

	Stage	Date
1	Submission of OBC to DEFRA	September 2006
2	OBC approval	January 2007
3	OJEU notice published	February 2007
4	Information Pack and PQQ issued	March 2007
5	Issue Invitation to Participate in Dialogue	July 2007
7	Call for Final Tenders	November 2007
8	Tender evaluation	December 2007 to May 2008
9	Announce Preferred Bidder	June 2008
10	Due diligence	September 2008 to November 2008
11	Contract sign off	November 2008
12	Commencement of contract	December 2008

LATS Strategy

11. The reference project is based on waste flow projections using 2003/04 data. Because of the complexity of the costing and financial modelling it has not been possible to update to more recent data. However, the implications of basing the reference project on 2003/04 data have been tested and have been shown to be relatively immaterial over the life of the project, although the implications are significant to short term LATS demand. A report was submitted to the Environment and Sustainability EMAP setting out the CYC LATS (landfill allowances) position in November 2005; this showed that by 2008/09 the Council would be landfilling more waste than it had been allocated in Landfill Allowances. As such, CYC would be subject to LATS penalties unless additional actions such as recycling were undertaken. Further work is ongoing and it is intended to report to the Executive in Autumn 2006 on the LATS position and strategy for York.

12. The OBC assumes that the Councils will be in deficit for LATS from 2008/2009 to 2012/13.

Competitive Dialogue

13. DEFRA are anticipating that the competitive dialogue process, recently introduced, will be used for the PFI procurement. The impact of this is that the 'dialogue' will take place earlier in the process than under traditional PFI contracts, thus causing additional bidding costs for potential contractors. Further discussions are being held prior to making a final decision on the use of this process.

Value for Money/Affordability

14. As set out above, the OBC compares the cost of 'status quo' – ie continuing with the existing service provision and accepting landfill tax, LATS penalties, and the 'reference project' as described above. Both capital and revenue costs have been taken into account and a net present cost calculated. A significant number of assumptions have been built into the financial modelling, including assumptions on LATS penalties and the trading value of LATS. Costs are compared using procurement through a conventional approach Public Sector Comparator, (PSC) and PFI funding. In accordance with Treasury Taskforce guidance a qualitative and quantitative assessment is required. In addition sensitivity analysis is required by the Treasury to ensure the assumptions and business case are robust. The results of the analysis are set out in the Executive Summary.
15. The cost of the Reference Project has been established as £195M lower than that of the status quo over the life of the Project. This calculation illustrates that the Reference Project offers value for money as part of the options appraisal.
16. The OBC also compares the cost of the reference project and assumed PFI support to projected budgets in order to determine the 'affordability gap'. All options including the status quo will cost considerably more than the Council now pays for dealing with the City's waste. The latest estimate of the 'affordability gap' is set out at table 6.7 in the Executive Summary. The table identifies the 'gap' for the whole project and for Years 1 to 6 that the two Councils will share, should the costs envisaged in the model be the true costs of the contract and the other local methods of dealing with waste. The table shows a significant increase in costs in 2008/09 and further increases each year until there is a further very significant increase in 2013/14 as the main facilities for residual waste treatment are projected to come on stream.
17. Both Councils will seek to profile the increased costs and to 'smooth' the increases required year on year to ensure they can be contained within annual overall Council Tax increases. The impact on City of York Council budgets will be very significant and a significant reprioritisation of budgets and spending towards waste management and away from other services will be necessary.
18. The conclusion as stated in Section 1.6 of the Executive Summary, is that the Councils recognise the necessity to allocate resources sufficient to make the project affordable over the life of the contracts, subject to any further obligations and financial parameters as directed by DEFRA or any other Government department. This is on the basis that the projected costs of the project are

considerably less than the costs of doing nothing. However, in providing this commitment it should be noted that the reference project does not represent the least cost option, but has been proposed as the 'best' option of those evaluated, having regard to all the issues including cost.

Sites and Planning

19. This is the issue seen by DEFRA as the most critical in the delivery of waste PFI projects. The Councils are working together to identify potential suitable sites and to ensure they are considered as part of the emerging Local Development Frameworks. An initial site search has identified a number of potentially suitable sites for the range of infrastructure requirements across the County. These are being reviewed with a view to NYCC securing sites sufficient to deliver the project. These sites can then be made available to all bidders on an equal basis thereby increasing the likely number of bidders.
20. Work on developing planning applications for transfer stations and other front-end services will begin as soon as sites are secured. It is currently proposed that planning applications for treatment plant will be delayed until after appointment of a preferred bidder although significant pre-planning assessments will be conducted in order to give bidders greater comfort that a successful planning application is possible. However, it is proposed to ensure that a minimum of 2 strategically located sites, suitable for development as treatment plants, are secured and made available to all PFI bidders. It is unlikely that any suitable sites will be identified within the City of York boundary. The project officers are maintaining close contact with the Councils' planning teams to ensure a high degree of co-ordination is achieved in relation to the Local Development Frameworks. Updates on sites and planning issues will be brought to the Executive in due course.

The Role of Yorwaste

21. The Councils' jointly own the Local Authority Waste Disposal Company (LAWDC) Yorwaste. Yorwaste owns or controls a number of strategically placed sites and is the main waste management contractor for both NYCC and CYC. Yorwaste also provides services to other Local Authorities within North Yorkshire and the Region.
22. Following extensive evaluation, it has been concluded that it is not in the Councils' interests for Yorwaste to bid for the PFI residual waste treatment contract. This is due to a range of issues but primarily because of the likely impact Yorwaste's involvement will have on competition and the potential for prejudicing the award of PFI credits (due to a lack of risk transfer and impact on competition). However, it is anticipated that Yorwaste will participate in the competition for waste handling and recycling services subject to normal competitive procurement processes.

Partnership Arrangements

23. There is already a joint working agreement (JWA), in place between NYCC and CYC with regards the PFI procurement. In addition both Councils (and the NY district & borough Councils) have all approved the JMWMS. NYCC and the NYCC districts & boroughs have a 'statement of agreed principles', which is being developed into Service Level Agreements (SLA's). These will result in

guarantees of recycling performance, agreed collection methodology, agreed delivery points (transfer stations), waste analyses being undertaken and joint waste minimisation initiatives. As a collection authority, CYC will need to ensure it has similar delivery standards for its collection arrangements.

24. NYCC will be the lead authority in the procurement and CYC and NYCC will agree a financial allocation mechanism to ensure an equitable allocation of financial and legal obligations under the PFI contract. Initial work has taken place on this and will be concluded as part of the contractual arrangements.

Corporate Priorities

25. The Council has recently agreed Improvement Statements, as part of the Council Plan. IS1 is 'to decrease the tonnage of biodegradable waste and recyclable products going to landfill'. This project addresses the action 'to undertake a review and audit of the amount of waste generated and disposal methods, of waste from Council activities'.

Implications

26. The following implications apply.

- **Financial**

27. There are extremely significant financial implications for this project. External financial advisors have been employed to ensure appropriate advice is received. In addition the Director of Resources is on the Strategic Project Board. The CYC waste disposal budget is made up as follows: -

	2005/06 £000	2006/07 £000
HWRC management and disposal	629	553
HWRC transfer and processing costs	375	226
Residual waste disposal	1,087	1,258
Landfill tax	1,661	1,751
Recycling credits	459	459
Annual waste disposal budget	4,211	4,247
Budget not available for reference project	N/A	-459
Available budget for reference project	N/A	3,788

28. The net budget assumed as available for delivery of the Reference Project is therefore £3,788k. North Yorkshire County Council have similarly identified an existing budget of £12,671k. These figures have been inflated by 2.5% year on year (thereby ignoring the effect of waste growth, LATS and landfill tax increases) and form the basis of the available budget for comparison with the projected costs of the reference project. It should be noted that landfill tax is budgeted at £21/tonne in 2006/07 and will rise by £3/tonne annually until it reaches £35/tonne in 2011/12.
29. The net impact of the Reference Project on the budget for CYC alone is identified in the Table below (based on the 2003/04 waste flow projections,

rather than updated projections at this stage). This assumes a split between NYCC and CYC on the basis of assumed waste tonnages, which will require further analysis. The figures set out below included LATS.¹

	06/07	07/08	08/09	09/10	10/11	11/12	12/13	13/14
	£000	£000	£000	£000	£000	£000	£000	£000
Total Reference Project cost	3,788	3,883	7,919	9,468	11,004	11,718	12,650	13,256
Budget PFI Credits	-3,788	-3,883	-3,980	-4,079	-4,181	-4,286 -566	-4,393 -566	-4,503 -1,303
Budget Gap	0	0	3,940	5,389	6,823	6,867	7,692	7,451
Council Tax Increase	0%	0%	6.2%	2.1%	2.6%	0.1%	1.4%	-0.6

(It should be noted that the significant increase in costs in 2008/09 occur as recycling and transfer infrastructure are brought on- stream).

30. Both Councils will seek to profile the increased costs and to 'smooth' the increases required year on year to try to ensure they can be contained within annual overall Council Tax increases. As identified in the table above the impact on City of York Council budgets will be considerable and a significant prioritisation of budgets and spending towards waste management and away from other services will be necessary.
31. As stated earlier in the report there are a significant number of assumptions. One of the key assumptions is the trading value of LATS permits. These are as follows: -

Years	Landfill allowance trading price (£/t)
2005/06 – 2007/08	30
2008/09 – 2009/10	70
2010/11 – 2012/13	120
2013/14 – 2018/19	100
2019/20 – 2024/25	75
2026/27 – 2032/33	50

32. LATS penalties will be at £150/t for each tonne of biodegradable waste the Council landfills in excess of allowances held (after leasing, borrowing or trading). If CYC landfills 10,000 tonnes in excess of its allowances in 2009/10 will cost £1.5m.

- **Human Resources (HR)** – there are no HR implications.

¹ The decrease in estimated costs in 2013/14 relates to the assumption that there will be surplus LATS allowances. If this does not prove to be the case there will be a significant increase in cost in that year.

- **Equalities** – there are no equalities implications.
 - **Legal & Procurement Implications**
33. The PFI process is a complex legal and procurement exercise. As such legal advisors have been employed to advise the project team. In addition the Head of Civic Democratic & Legal Services attends the Internal Waste Board and is involved in the project as needed. The standard 4Ps procurement pack is being followed to ensure appropriate procedures are followed, and the corporate procurement team is kept up to date with ongoing developments.
- **Crime and Disorder** - there are no crime and disorder implications.
 - **Information Technology (IT)** – there are no IT implications.
 - **Property** – there are no Property implications.
 - **Other** - there are no other implications.

Risk Management

34. There are clearly significant risks in a project of this magnitude and complexity. As a result, specialist risk management consultants have been identified and will be engaged as part of the project procurement team. In addition this project is ranked as a high risk on the strategic risk register. Detailed risk analyses have been carried out as part of the options appraisals work, as set out in the Executive Summary. At this stage, any commitment to submit the Outline Business Case does not in itself present significant risk. A more detailed assessment of the risks of the project will, however, be brought to the Executive when DEFRA have responded to the Outline Business Case.

Way forward

35. (a) The OBC sets out NYCC and CYC's business case for the procurement of residual waste treatment. The revised procurement strategy is based on: -
- Joint procurement of residual waste treatment only, funded through PFI funding (the technology to be determined through the procurement process).
 - Each Council will procure other front-end services and landfill services separately and independently.
 - In the event of PFI funding not being available, joint procurement to be pursued using alternative funding (PPP or prudential borrowing).
- (b) The OBC offers value for money in accordance with Treasury Task Force guidance and the Councils need to be committed to finding the additional resources to fund this project.
- (c) To advise Yorwaste shareholders that Yorwaste be requested not participate in the residual waste treatment contract.

Recommendations

36. The Executive is requested to
- a. Approve the delegation of submission of the Outline Business Case to DEFRA as a bid for PFI funding to the Director of City Strategy based on the attached Draft Executive Summary of the OBC.
 - b. Confirm that the Council recognises the necessity to allocate resources sufficient to make the project affordable over the life of the contracts, subject to any further obligations and financial parameters as directed by DEFRA or any other Government department.
 - c. Confirm the residual waste treatment project offers value for money to the City of York Council.
 - d. Confirm that Yorwaste be requested not to participate in the PFI residual waste treatment contract.
 - e. Note and support the approach to sites and planning issues.
 - f. Note that delivery standards for CYC collection services will need to be achieved to interface with the PFI contract.

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Report Approved **Date** 31 August 2006

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Report Approved **Date** 31 August 2006

Wards Affected:

All

For further information please contact the author of the report

Annexes:

Annex 1 – York & North Yorkshire Waste Management Partnership, Waste PFI Outline Business Case Executive Summary – September 2006.
Annex 2 – Total Waste 2005/6 diagram

Background Papers:

York and North Yorkshire Waste Management Partnership Waste PFI Project Outline Business Case

Previous reports to Executive:

- Joint Waste Management Strategy Report
- Legal Agreement with NYCC

Glossary of Terms

JMWMS	Joint Municipal Waste Management Strategy
OBC	Outline Business Case
NYCC	North Yorkshire County Council
CYC	City of York Council
JWA	Joint Working Agreement
PFI	Private Finance Initiative
DEFRA	Department of Environment, Fisheries and Rural Affairs
BPEO	Best Practical and Environmental Option
4Ps	Public Private Partnership Programme
MBT	Mechanical Biological Treatment
EFW	Energy From Waste
PPP	Public Private Partnership
SRF	Solid Residual Fuel
LATS	Landfill Allowance Trading Scheme
PSC	Public Sector Comparator
SLA	Service Level Agreement
LAWDC	Local Authority Waste Disposal Company
WCA	Waste Collection Authority
WDA	Waste Disposal Authority
HWRC	Household Waste Recycling Centre
SOAP	Statement of Agreed Principles