

CABINET

27 SEPTEMBER 2016

GATEWAY 1 PROCUREMENT COMMENCEMENT: HOUSEHOLD WASTE RECYCLING CENTRES

Portfolio Holder: Councillor Phil Filmer, Front Line Services

Report from: Richard Hicks, Director of Regeneration, Community, Environment and Transformation

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SUMMARY

This report seeks approval to commence the progression of the recommended management option partner for the Household Waste Recycling Centres.

The management options have been approved for submission to the Cabinet after review and discussion at the RCET Directorate Management Team Meeting on 4 August 2016 and the Procurement Board on 31 August 2016.

The RCET Directorate Management Team and Procurement Board have recommended that this project be approved as high risk procurement.

1. BACKGROUND INFORMATION

1.1 Service Background Information

1.1.1 The current contract for the three household waste & recycling centres (HWRCs), run by FCC, is due to expire on 30 September 2017 but has an option to be extended for a further two years if agreed by both parties.

1.1.2 Under the terms of the contract, FCC shoulder the full risk on the market value or cost of the majority of waste streams accepted at Medway's HWRCs. These values/costs have changed significantly since contract inception and FCC will not accept an extension on the same terms unless the management fee is increased.

1.1.3 Four options are being put forward to Cabinet for running the HWRCs post-September 2017. This report sets out the high level principles of the following options:

Option	Proposal
1	Procure a new contract to start October 2017
2.a	Medway grants FCC a contract extension on the same, existing terms
2.b	Medway grants FCC a contract extension but agrees to share the risk on the cost/value of certain wastes
3	Enter into a joint venture with Medway Norse and share the risk on the cost/value of certain wastes.

1.1.4 As part of these proposals, it should also be noted that the sites are now old compared to many modern facilities. It is therefore proposed that the HWRC provision undergoes detailed scrutiny to ensure it can return best value for Medway and its residents in the long term. This should include a stocktake of the location and suitability of each site and how well they cope with the demands of a growing population and a frequently-changing waste industry.

2. PROCUREMENT DEPENDENCIES & OBLIGATIONS

2.1 Legal Duty and Current Provision

2.1.1 Under the EPA 1990, Section 51, Waste Disposal Authorities (WDA) have a duty to provide HWRC facilities, however, there is no mention of the number needed as long as they fulfil the requirement to '*be reasonably accessible to persons resident in the area*'. This also means that not all facilities need to be provided at all sites.

2.1.2 Under the Controlled Waste Regulations, local authorities are not obliged to accept commercial waste, tyres or construction waste, such as doors, windows, rubble, plasterboard, soil etc. The deposits of such waste can be restricted and/or a fee charged to accept them if an authority so wishes.

2.1.3 Medway's three sites are currently licenced to accept waste from households only.

2.1.4 Medway currently has no restrictions or charges in place regarding the amount of waste householders bring in to the sites by car and trailer.

2.2 Market Analysis

2.2.1 Under the current contract, costs for disposal/recycling and any income from material sales, except for wood and residual waste, falls to the contractor. Medway pay a fixed management fee (uplifted by RPIX annually) designed at time of tender to reflect the expected tonnages and resulting costs/income for materials deposited during the life of the contract. This has put the majority of risk onto the contractor. Markets for recyclable material have taken a significant down turn since the

contract's inception in 2010, meaning the contractor has not achieved the financial returns they projected.

- 2.2.2 Soft market testing and benchmarking (see Exempt Appendix) undertaken by Waste Services and Category Management strongly suggests that poor competition and high pricing will result if Medway attempt to procure on the same contract terms as it did in 2010.
- 2.2.3 With recent volatility around the market value of materials, waste management companies are beginning to decline contracts where they shoulder all the financial risk on what people throw away. Soft market testing of several potential HWRC operators last year, strongly suggested any contract seeking to pass 100% of this risk to the operator would either not receive bids or have its cost very heavily front-loaded.
- 2.2.4 The simplest form of risk share is a straight 50/50 split in the losses or profits affected by fluctuations in market prices, being determined by an agreed base price and measured thereafter by a set of suitable indices or open-book accounting. It is impossible to predict the full exposure of this risk but the analysis in the exempt appendix looks at the indicative financial outcome from 2011 to 2016 resulting from changes in market prices.
- 2.2.5 It is important to note, in a risk share agreement, income or pressure can be generated according to the change in the market value or cost of processing waste. Using the examples in the exempt appendix, it can be seen that, overall, an income would have been enjoyed during 2011/12 but a pressure would have been suffered last year. Budget builds involving this type of arrangement would need to take account of this uncertainty.

3. BUSINESS CASE

3.1 Procurement Project Outputs / Outcomes

As part of the delivery of this procurement requirement, the following procurement project outputs / outcomes within the table below have been identified as key and will be monitored as part of the procurement project delivery process. It should be noted that once an option has been chosen, further outputs and outcomes can be worked on also.

Outputs / Outcomes	How will success be measured?	Who will measure success	When will success be measured?
1. Value for Money	In an ever changing market, the Council needs to be able to adapt to avoid deploying services which do not work. By analysing historic trends we can identify benefits arising from the change in service and ensure we are providing value for money solutions	Waste Services	Annually
2. Innovation	Due to the changing market, the Council needs to adapt and provide innovation to ensure it remains environmentally sustainable. This will be measured by comparing the current provision against the future provision; similarities and differences can then be compared.	Waste Services	Annually
3. Sustainability	What is currently offered by the Council is not financially sustainable so a happy medium needs to be contracted. Success will be measured by adapting the current service to which still enables all residents' fair access on a continued basis.	Waste Services	Annually
4. Improving Service Delivery	Medway has historic KPIs relating to the recycling rates and customer satisfaction levels at all 3 sites. Success going forward will be measured by comparing historic data against future targets.	Waste Services	Annually

3.2 Project Management

- 3.2.1 The procurement project management will be met via internal resource, mainly those from category management and waste services. Post award, the contract will be managed, on a day to day basis, by the waste services team. Contractual disputes will be assisted by the category management team.

4. OPTIONS

4.1 Summary of Options

Option 1: procure new contract for October 2017

- 4.1.1 The materials market took a further dramatic downturn during last year, which prompted Waste Services to carry out a soft market testing exercise to gauge its affect on procuring HWRC management. From the intelligence gathered, outlined within the exempt appendix, it is the officers' view that, to gain competitive and realistic tenders, any new contract let in the foreseeable future will need to look significantly different to the one currently let by Medway. Typical alterations would include:

- A payment mechanism that at least shares the risk of fluctuations in the market value/cost of dealing with certain materials.
- Either restrict the deposits of certain waste streams or take greater responsibility for their disposal cost.

- 4.1.2 There is insufficient time to compile and agree such a change in specification ready for a full procurement. In order for a new contractor to be mobilised and ready to take on the sites from October 2017, the contract would need to be awarded no later than April 2017. Should Medway procure this service on its existing specification, the final outcome carries an operational and financial risk of failure.

Option 2a: extend current contract with FCC

- 4.1.3 FCC has clearly stated that the contract as it stands is not viable for them. In order to make a two-year extension viable and continue with FCC taking all risk on the cost/value of wastes, the annual management fee proposed is substantially higher (as outlined within the exempt appendix).

Option 2b: extend current contract with FCC but share risk

- 4.1.4 FCC has proposed a lower management fee to extend the current contract for two years if Medway agree to share the risk on the cost/value of wastes. In this instance, the proposed annual management fee is contained within the exempt appendix. The total cost of running the HWRCs, however, will be influenced by the risk share arrangement. Under current market conditions, this would be a further pressure.

Option 3: enter into a joint venture with Medway Norse but share risk

4.1.5 Medway Norse has proposed a management fee to run the HWRCs but share the risk, via open-book accounting, on the cost/value of wastes. The annual management fee they have proposed is not dissimilar from that of the incumbent (as outlined within the exempt appendix). The total cost of running the HWRCs, however, will be influenced by the risk share arrangement. Under current market conditions, this would be a further pressure.

4.2 Summary of Options

4.2.1 A summary of options, outlining the financial implications of the above options, can be found within the exempt appendix.

4.3 Supplier Analysis

4.3.1 Thorough supplier analysis has been conducted to ensure that the options put forward are lucrative to the authority and sustainable going forward. A breakdown of such can be found within the exempt appendix.

4.4 Review of options

Option 1

4.4.1 In order to ensure competitive pricing, certain political decisions around the service provision will need to be made and written in to a new contract specification. These would definitely need to include a risk share arrangement and, for Medway to have more confidence it would receive lower prices than options 2b and 3, other service reductions such as waste limits, charging or closing certain sites on certain days would need to be considered. The procurement timetable is far too tight to achieve this.

Option 2a

4.4.2 FCC has stated their price for extending the contract on the same terms, includes an additional mark-up to offset the market risk on the cost/value of wastes. Soft market testing suggests this would be a typical response from any other contractor. The proposal provides for a 2-year 'business as usual' solution but will have a definitive cost increase as outlined within the exempt appendix.

4.4.3 By taking this option, it is only likely to postpone the need to agree the type of service changes mentioned in Option 1, if costs are to be reduced after October 2019, when the extension would expire.

Option 2b

4.4.4 Within this risk sharing option, FCC is willing to work with Medway to develop a price tariff for trade waste and implement the provision. This may help reduce and offset the cost of trade waste that currently gets in to the sites undetected and would be a service improvement. Other cost saving measures, such as limiting the amount of certain wastes residents

can deposit or closing sites on less busy days, would need to be agreed in advance of the extension in order for FCC to plan for that cost saving.

- 4.4.5 FCC have offered a further, unspecified discount if Option 2b is taken up prior to October 2019.

Option 3

- 4.4.6 The option to move HWRC into the Joint Venture (JV) with Medway Norse is timely and convenient for its purpose. The proposed management fee and risk share arrangement is very similar to that of option 2b and the expiry date of the JV arrangement will coincide with the end of the serviceable life of any new fleet. There are also some unrelated opportunities for the JV in terms of utilising some space that could be made available at the Cuxton or Capstone sites.
- 4.4.7 Norse run the majority of HWRCs in Norfolk on behalf of the County Council. Their sites have been visited by various officers of the Council.
- 4.4.8 Within the Norse group there is materials trading arm called NEWS. This gives Medway Norse greater confidence in being able to trade recyclables competitively and find the necessary outlets for the disposal of other wastes. Should a trade waste tariff be implemented, this option allows for that to happen.
- 4.4.9 The 'open-book accounting' method offered by the JV is probably the best way of measuring any risk share arrangement and the flexibility the partnership has will make any cost saving policy or service changes far easier to implement during the contract period.

Conclusion

- 4.4.10 Once a partner has been chosen, Medway will work with that partner to consider measures that will reduce either the management fee and/or exposure to risk and formulate further option reports.

5. RISK MANAGEMENT

5.1 Risk Categorisation for all options

1. Risk Category: Procurement Process	Likelihood: Significant	Impact: Critical
Outline Description: Due to the limited number of options at the Council's disposal, if a decision is not taken as soon as possible it may impact the outcome.		
Plans to Mitigate: Implement and adhere to a strict timetable from date of decision through to contract start.		
2. Risk Category: Financial	Likelihood: Low	Impact: Significant
Outline Description: Because of the changes in the market since the current contract was awarded, there are significant changes that need to be implemented on any contract going forward. Failure to fully utilise the Council's leverage could result in financial increases not envisaged at the options appraisal stage.		
Plans to Mitigate: Early approval will give officers the greatest time to negate any financial risks which may have otherwise arisen.		
3. Risk Category: Reputation	Likelihood: Low	Impact: Critical
Outline Description: If service changes are made there could be implications for the general public.		
Plans to Mitigate: Any changes will be communicated with all members of the general public so they are aware of what will change and when. This will help mitigate any inflated risk of complaints.		

6. CONSULTATION

6.1 Procurement Board

6.1.1 Procurement Board considered this report on 31 August 2016 and supported the proposed approach set out in the report.

6.2 Internal (Medway) Stakeholder Consultation

6.2.1 To ensure the outcome is palatable, monitoring meetings will be held for all applicable stakeholders.

6.3 External Stakeholder Consultation

6.3.1 Depending on the partner chosen, the outcomes proposed and progressed will be compared to external arrangements to ensure value for money solutions have been made.

7. SERVICE IMPLICATIONS

7.1 Financial Implications

7.1.1 The procurement requirement and its associated delivery (as per the recommendations at Section 9, will be funded from existing revenue budgets.

7.1.2 Further detail is contained within Section 2.1 Finance Analysis of the Exempt Appendix.

7.1.2 Due to the financial implications, namely the potential forecast overspend against the current arrangement, finance wish to seek certainties prior to any awarded contract of how the budget pressure will be met and assist in setting the applicable index for inflation. It is therefore proposed that, where necessary, the finance team forms part of the negotiation panel to assist in achieving the Council's contractual objectives.

7.2 Legal Implications

7.2.1 The Council is under a statutory duty to collect waste paper, metal, plastic and glass separately where it is necessary to ensure recycling and it is technically, environmentally and economically practicable. This duty arises when making arrangements for the collection of waste, which includes the collection of waste at HWRCs (if the Council does not already collect these waste streams separately).

7.2.2 The Council is not subject to any government imposed recycling targets. However the Council's Waste Strategy for 2005 to 2020 aims to increase recycling rates to 55% by 2020. Officers will need to consider this aim in the planning of future HWRC services.

7.2.3 If a longer planning or mobilisation period is required by officers in relation to delivering the chosen options, officers should explore the possibility of

utilising option 2b for a shorter contract extension to guarantee the immediate delivery of services and also to test pilot a risk sharing arrangement.

7.3 TUPE Implications

- 7.3.1 There are likely to be TUPE implications if the current contractor has a dedicated workforce for the provision of services at the Council's HWRCs. Any employees assigned to the HWRCs will automatically transfer to a new operator under the service change provisions of the TUPE Regulations 2006.

7.4 Procurement Implications

- 7.4.1 As highlighted within this report, it is important to select an appropriate partner who will be able to work with the Council to develop sustainable practices. It is clear that from whatever route is taken, changes are necessary and therefore care and consideration needs to be taken as to what implications these will have and any detrimental effects are limited as far as possible within reason.
- 7.4.2 Any contract would be expected to start on 1 October 2017, therefore a decision is crucial to enable progression towards an acceptable replacement.
- 7.4.3 Paragraph 1.8.2.8 (Teckal Exemption) of the Council's Contract Procedure Rules allows the award of contracts between contracting authorities and controlled entities, in this case the Council and Medway Norse.

7.5 ICT Implications

- 7.5.1 ICT do not currently provide any services to any of the household waste recycling centres.

8. OTHER INFORMATION

- 8.1 Medway needs to ensure that the quality of service is maintained whilst also adapting to the changes in market. It is evidenced, by the market, that the current contract is not sustainable and to ensure public money is spent in the best possible way, changes will need to be explored and agreed.

9. RECOMMENDATION

- 9.1 The Cabinet is asked to approve Option 3, in accordance with the Teckal exemption Medway Council can execute with Medway Norse, for the future service delivery of the Household Waste Recycling Centres.

10. SUGGESTED REASONS FOR DECISION

- 10.1 This will enable negotiations to be undertaken with Medway Norse to achieve the best outcome for the Council.

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APPENDICES

Exempt Appendix

BACKGROUND PAPERS

None