

Name of Cabinet Member:

19th October 2010

Councillor Lindsley Harvard

Directors Approving Submission of the Report:

Director of City Services and Development

and

Director of Finance and Legal Services

Ward(s) affected:

All Wards

Title:

Project Transform – Withdrawal from the PFI Procurement Process.

Is this a key Decision?

Yes

The decision to be made by Council is to endorse the recommendation of the Project Transform board to withdraw from the PFI procurement process on the grounds of value for money following the outcome of the independent engineering report which assessed the life span of the existing Energy from Waste plant and affordability of the PFI option versus the alternatives.

Executive Summary:

The decision to participate in a sub-regional procurement of a new residual waste treatment facility was taken by Council in October 2008. In addition to approving the PFI procurement process the Council also mandated officers to continually review all options for the future provision of residual waste treatment facilities in Coventry and the wider sub-region, to ensure that the PFI option represented the best value for money.

This report and recommendations are the result of this review process.

Recommendations:

That Council:

1. Withdraws from the PFI procurement for a new sub-regional residual waste treatment facility and delegates to officers the authority to take all steps necessary to facilitate the withdrawal.
2. Based on the Outline Business Case (OBC) forecast, notes the estimated costs avoided (the affordability gap) to Coventry of £4.5million per annum from 2015/16, achieved from not proceeding with the procurement of a new facility.
3. Endorses the decision taken by Council on the approach of sub regional planning and organisation of waste disposal.
4. Confirms the dissolution of the Project Transform Members Advisory Panel.

Lists of Appendices included:

None

Other useful background papers:

None

Has it or will it be considered by Scrutiny?

No

This report will go directly to Council given the city wide impact and level of financial decision.

Has it, or will it be considered by any other Council Committee, Advisory Panel or other body?

Yes

The same decision is being taken by Solihull Metropolitan Borough Council at their meeting on 12th October 2010. In addition Warwickshire County Council will be considering the implication of this decision at some point after the 19th October 2010.

Will this report go to Council?

Yes – 19th October 2010

Report Title: Project Transform – Withdrawal from the PFI Procurement Process.

1. Background:

- 1.1 The Council, together with its Partners (Solihull MBC and Warwickshire CC), has long recognised the challenges facing it in terms of providing a sustainable and cost effective solution to its long-term residual waste treatment requirements.
- 1.2 At present, the Council's residual waste is treated at the existing energy from waste facility on the London Road. This facility is operated by the Coventry and Solihull Waste Disposal Company which is owned by the Council (two thirds shareholding) and Solihull MBC (the remaining one third shareholding). The facility was constructed in the mid 1970s. Over its period of operation it has been significantly up-graded to meet changing waste management needs.
- 1.3 In order to ensure that the Council had a long-term solution and due to the fact that any solution would take ten to twelve years to become operational, the Council in 2005, jointly with Solihull MBC commissioned an independent condition survey of the energy from waste treatment facility to determine its remaining economic life (as it was approximately 30 years old). The survey determined that the existing facility had a life of between fifteen and twenty years (i.e. until approximately 2020) with the minimal levels of on-going maintenance provided in 2005.
- 1.4 Over the next few years, the Council in response to the condition report continued to examine its options for delivering a sustainable long-term solution. In 2007, the Council and Solihull MBC commissioned external financial advisors to complete a financial options appraisal to determine the best financial solution for the Councils. This report considered the findings of the condition survey and benefits to the two shareholders of joint working with Warwickshire County Council (WCC) to develop a long-term solution. The study concluded that joint working between the three Councils would bring significant economies of scale. In addition, the study stated that a joint project, involving sub-regional working to develop a sustainable solution, would be very likely to attract Private Finance Initiative (PFI) credits from the Department for the Environment Food and Rural Affairs (Defra).
- 1.5 The three Councils therefore agreed in late 2007 to submit an expression of interest (EOI) to Defra for PFI credits to develop a sub-regional waste treatment solution. The EOI was formally submitted to Defra in March 2008 and was successful in gaining Defra support to proceed to the next stage of the process (the development of an Outline Business Case). Whilst this EOI demonstrated a considerable level of government support in the form of PFI credit it also identified a funding gap for Coventry of £1m per year from the start of the new facilities operation. This PFI bidding round was presented at the time as the last opportunity to get central government financial support for waste disposal projects. This made it a very important opportunity to pursue.
- 1.6 To strengthen the basis for joint working, in December 2007, the three Councils agreed a two year memorandum of understanding to work together to develop joint solutions in all areas of waste management where this was mutually beneficial. It was also agreed that the project to develop a sub-regional residual waste treatment solution would be branded 'Project Transform'. At the same time the Councils agreed to the formation of a Members Advisory Panel, comprising 3 elected members from each authority. This panel has no decision making powers and was established to both support and challenge the development of Project Transform.

- 1.7 Following the approval of the EOI, the three Councils commenced the development of an Outline Business Case (OBC) for PFI credits.
- 1.8 The three Councils entered into a joint working agreement on the 30th October 2009 which detailed how we would work together with Coventry City Council acting as lead authority.
- 1.9 The petition raised on 6 July 2010 by Cllr Nellist with 17 signatures on the subject of the PFI project will be considered under this item on the Council agenda of the 19th October 2010.

2. Project Transform - Outline Business Case

- 2.1 The OBC, through a process of option appraisal, determined that a Combined Heat and Power Energy from Waste (CHP EfW) facility located on a site adjacent to the existing facility, in Coventry, best met the requirements of the partnership.
- 2.2 The costs of the construction and operation of such a facility (known as the reference project), over the twenty five year period (2016 to 2041), were forecast at £1 billion with £260 million attributable to the construction of the new facility. Within the OBC the Council was required to compare the estimated costs of a new PFI facility with a do minimum scenario in order to demonstrate value for money of the PFI solution. The do minimum scenario assumed that the Council would use the existing EfW until it ceased to operate in 2020 and then send 305,000 tonnes of sub-regional residual waste to landfill (c100,000 tonnes pa for Coventry). This would be at a significant additional cost to that currently being paid for waste disposal and the estimated costs under a PFI solution. The OBC therefore demonstrated that the PFI was the best solution compared with the alternative of landfill, given the information available on the lifespan of the existing plant.
- 2.3 The OBC demonstrated a predicted affordability gap for a new residual waste treatment facility. The difference between the estimated costs of the residual waste treatment facility and existing budgets for the Council was an affordability gap of £4.5 million per annum (for 2015/16) and onwards. This figure is after taking into account the benefit to Coventry from the PFI credit.
- 2.4 Experience from earlier residual waste treatment projects has been that it has been challenging and time consuming to gain planning permission for these facilities. It was therefore agreed that the Partnership would seek outline planning permission on the selected site, adjacent to the existing facility, early in the procurement process. This would also create greater certainty for the bidders in respect of the delivery of the site and hence significantly reduce the risk premium included within their price.
- 2.5 The OBC was submitted in October 2008. In June 2009, after scrutiny by Defra and HM Treasury, Project Transform was awarded £129 million of PFI credit, equating to £9.2 million per annum for the total project (£3.6m per annum for Coventry City Council), towards the costs of the Project.
- 2.6 In addition to approving the submission of the OBC and its associated financial implications, the Council resolved the following in October 2008:

'Endorse the recommendations of the Member Advisory Panel of Project Transform to require Officers to investigate possible alternative solutions to ensure that the PFI project represents best value.'

2.7 The procurement process was forecast to take three years with financial close in March 2012 and a permanent project team of eight staff, supporting by a wider group of officers and external advisors, was established during 2009.

3. Project Transform - Procurement Process and Costs

3.1 The OJEU European procurement notice was issued in September 2009 with the pre-qualification short-list being agreed in February 2010.

3.2 In December 2009, Cabinet approved the criteria to be used to evaluate the solutions submitted to meet the Project Transform partnership's requirements for its residual waste treatment needs.

3.3 The procurement process continued with the invitation to submit outline solutions issued to the pre-qualified companies/consortium in February 2010. The evaluation of the outline solutions was completed in June 2010 and it was planned to announce the results following formal approval by the Project Board in July 2010. This decision was delayed to allow the work on alternative options to conclude.

3.4 The cost of the procurement exercise and the development of the outline planning application up to 31 March 2010 is £1.7m of which the Council's share is £0.64m. Forecast costs for the 2010/11 financial year are c£0.6m of which the Council's share is c£0.26m.

4. Options considered - Alternatives to a PFI procurement for a new sub-regional waste treatment facility

4.1 Following the Council resolution in October 2008, officers have been working to better understand the alternatives to a PFI solution. This has included detailed financial work to assess the relative costs and benefits of funding the project using PFI, set against a variety of other financing options. These have been presented to elected members through a number of group meetings. The Council was mindful to work as quickly as possible to ensure that a decision on the future of the PFI scheme, now in procurement, could be made before significant investment from both the Councils and the private sector bidders in developing detailed PFI solutions at the next stage of the procurement process. However, the level of information required to inform a decision and the complexity of the work has, by its nature, taken time.

4.2 As work on the alternative options progressed, a number of factors further reinforced the need to assess the suitability of the PFI solution. These included:

- A changing landscape in relation to government funding post the general election including the implications of the imminent Comprehensive Spending Review (CSR) which will see significant reductions in local government funding. This will make the financing of a significant affordability gap of £4.5m per annum from 2015/16 much more difficult. The CSR also raises the risk that Defra funding for the project is withdrawn, requiring the Councils to establish an alternative to PFI in any event.
- In addition, the longer the existing plant can last without replacement, the longer the Council could delay the need to fund the affordability gap associated with a new facility and potentially benefit from payment of dividends from the existing CSWDC.

- The Regional Spatial Strategy has been abandoned, which means less certainty in terms of housing and waste flow projections, which would shape some of the key assumptions on the required size of a new residual waste facility.
- The limited ability to consider alternative technology options as part of the PFI procurement due to the bankability of a EfW solution compared with other forms of emerging and less tried and tested alternatives. Delaying the decision to rebuild a facility would provide more time to consider these alternatives and for them to mature, in advance of the eventual rebuilding of a facility.

4.3 The exploration of financial options concluded that an updated independent engineering report was required to demonstrate if the existing EfW had a longer life than previously envisaged. If the existing plant could last beyond 2020, there was a very compelling financial case for the Council to withdraw from the PFI project. In late June 2010, the new Labour administration in Coventry asked officers to commission an independent engineering report. The Council, jointly with Solihull, commissioned SKM consultants to carry out the engineering study of the existing facility. The aim of this study was to assess the remaining economically useful life of the existing EfW plant and the levels of investment required to maximise its life. The results of the study were received in September 2010.

4.4 In summary the results of the SKM study are:

- The survey did not identify any aspect that requires major capital investment which may warrant the building of a new plant now.
- Given reasonable levels of ongoing investment and maintenance this could allow the plant to last until 2040 (with further life beyond this).
- The levels of investment required are c£60m 2010-2040 – based on known and expected legislative requirements.

4.5 This assessment is different from the results of the earlier (2005) engineering study, on which the decision to proceed with the procurement of a new solution was based, and therefore has led to recommendations in Coventry and Solihull that it represents better value for money to continue to operate the existing facility and to withdraw from the PFI procurement for a new solution.

4.6 The 2010 engineering report provides assurance that the plant can last well into the future. Initial work indicates that the capital investment required to keep the plant operational between 2010 and 2040 (c£60m) is likely to be met from within the existing CSWDC business plan based on the historical levels of annual investment. This means that there is not an affordability gap associated with this option, making it the best option in financial terms for the Council.

4.7 From the perspective of our sub-regional partners, the withdrawal from the PFI offers Solihull MBC the opportunity to benefit from its existing shareholding in CSWDC and avoidance of the PFI affordability gap. There is the opportunity for Warwickshire CC to continue to work closely with both Coventry and Solihull to explore collaborative approaches to waste strategy. Specifically, there is the opportunity for a meaningful dialogue to open between the CSWDC and Warwickshire County Council to explore cost effective solutions for waste disposal at the existing EfW, which will have significant surplus capacity post 2015 when current contracts end. This in turn secures contracts for the CSWDC going forward.

5. Timetable for implementing this decision:

The key deadlines for the implementation of this decision are:

- Official notification of Project Transform bidders – 20th October 2010.
- Official notification of Project Transform stakeholders including Defra – 20th October 2010.

6. Comments from the Director of Finance and Legal Services:

6.1 The decisions about when and how to replace the waste from energy plant at Whitley is an important one for the Council and has significant implications for the environment of the City and the Council's finances. In line with the Council recommendation in October 2008, officers have been working through the various financing options for a number of months culminating in the technical engineering report which confirms that the existing plant, with investment from the CSWDC at historical levels, can last up until at least 2040. This provides the technical evidence base that supports the financial case for withdrawing from the PFI.

6.2 The affordability benefits for the Council of withdrawing from the PFI and utilising the existing EfW are:

- Saving the affordability gap between our existing costs of waste disposal and those under the PFI at £4.5m per annum from 2015/16. The Council has set aside £0.5m in 2010/11, £1.5m 2011/12 and £2.5m 2012/13 in its Medium Term Financial Strategy to build up a fund to pay for these additional costs from 2015/16. The majority of this figure will no longer be required and can be used to assist the Council's financial position. There is an element of the initial 2010/11 allocation of £0.5m that has been used to fund some of the Council's share of the alternative options work and the engineering report, which will reduce the saving available in 2010/11 only.
- Savings between 2010 and 2013 of c£1m of procurement costs.

6.3 Subject to Council approval, further work is now required, working with Solihull Council, to ensure that the existing CSWDC continues to operate effectively. The decision to withdraw from the PFI offers the opportunity to work with CSWDC to review its governance arrangements and ensure that the company maximises its financial and service potential in the coming years. This includes the opportunity to extract dividends from the company. Options and recommendations will be brought back to Members for approval in the near future.

6.4 The withdrawal at this stage before the invitation to submit detailed solutions from the selected bidders is an appropriate time to withdraw and is a formal break point in the joint working agreement between the three authorities for Project Transform. This is before further significant costs are incurred by all the parties to continue with the competitive dialogue process.

7. Other implications:

None other than those covered in sections 8-13 of this report.

8. How will this contribute to achievement of the Council's key objectives / corporate priorities (corporate plan / scorecard) / organisational blueprint / LAA (or Coventry SCS)?

The disposal of municipal waste is a statutory function of Coventry City Council. This decision allows the continued safe disposal of municipal waste in a cost effective and environmentally beneficial way. In addition this decision will assist Coventry City Council in reducing the amount of carbon emitted from its processes compared to disposing of the city's residual waste at landfill.

9. How is risk being managed?

The main risks associated with this decision are:

No.	Risk	Mitigation
1	The delivery of the new facility using PFI procurement would have transferred a significant number of the risks of construction and operation to the selected contractor such as cost over-runs and the cost of diversion of waste should the facility be unavailable to accept waste.	<p>The action proposed in the SKM engineering report does not involve the construction of a new facility and considers that all proposed modifications / additions can be handled within acceptable engineering downtime.</p> <p>Coventry does have alternative tipping arrangements with a number of private sector landfill operators to manage short-term engineering downtime.</p>
2	In addition, the existing facility will be 65 years old in 2041 increasing the risk of reduced reliability.	Further proposals will be brought to the CSWDC shareholders before March 2011 on a proposed frequency of regular independent engineering plant inspections. These inspections will consider the age of the EfW and the need for any additional engineering work.
3	Responding to any future legislative changes that will now be the responsibility of the CSWDC – specifically in relation to emissions.	<p>The SKM report provides the shareholding authorities with a comprehensive list of expected legislative changes along with an operational / engineering solution.</p> <p>The continued periodic review of the EfW will allow the shareholding authorities sufficient time to respond to any unforeseen legislative changes.</p>

10. What is the impact on the organisation?

- 10.1 When formalised through the project board the disbanding of the Project Transform team will affect: 3 full-time posts, 2 part-time posts and one secondment. These will be managed through the council / partners security of employment agreements, in consultation with the trade unions.
- 10.2 The reputational risk to Coventry City Council with Defra on the returning £129m of PFI credit had been handled by early engagement with Defra's representative on the project board.

11. Equalities / EIA

There are considered to be no equality issues linked to this decision.

12. Impact for (impact on) the environment

- 12.1 This decision will maintain Coventry City Council's position as one of the lowest landfilling authorities in the UK. In addition the continued use of Energy from Waste as a treatment method will continue to represent a considerable carbon saving on disposing of the same amount of waste at landfill whilst continuing to generate sustainable electricity and potentially heat.
- 12.2 It should be noted that the existing Energy from Waste facility will be subject to the same stringent emissions controls as any new facility both now and in the future.

13. Implications for partner organisations

- 13.1 There is no adverse impact of this decision on Solihull MBC as the joint shareholders with the Council in Coventry and Solihull Waste Disposal Company.
- 13.2 Future consideration needs to be given on how Coventry, Solihull and Warwickshire can work together to deliver greater joint working in waste treatment / disposal. In particular the continued treatment of Warwickshire County Council's waste in the existing Energy from Waste facility post 2015 (the end of their current contract).

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