Department for Environment, Food and Rural Affairs

Review of Local Authority Waste Disposal Companies and Their Role in Future Procurement

Final Report

19297/IH/JB/OT November 2005

Jacobs Babtie 95 Bothwell Street, Glasgow G2 7HX
Tel 0141 204 2511 Fax 0141 226 3109

Department for Environment, Food and Rural Affairs **19297/IH/JB/OT**

Review of Local Authority Waste Disposal Companies and Their Role in Future Procurement

Final Report Issue

This report is approved for issue outwith the Company

.. **Project Director**
Ian Higham

Issue History

Date	Revision	Status
26 September 2005	Draft V2.0	Draft for comment
18 October 2005	Final Draft	Final draft for comment
15 November 2005	Final	Issue

Jacobs Babtie
95 Bothwell Street
GLASGOW
G2 7HX

Controlled Copy No: ….

EXECUTIVE SUMMARY

Introduction

This report presents the findings of the Review of Local Authority Waste Disposal Companies and Their Role in Future Procurement, which has been prepared by Jacobs Babtie on behalf of Defra.

The Research

The research was undertaken in two parts. The first part consisted of identifying and interviewing all existing Local Authority Waste Disposal Companies (LAWDCs) in England, their parent Waste Disposal Authorities (WDAs) and other key stakeholders in the waste procurement process, including financing bodies, financial advisors, legal advisors and Government and industry bodies. The findings from all these interviews were then analysed and collated into an interim report.

The second part of the research involved investigating the key issues identified in the interim report via a workshop held with invitees from the previously mentioned stakeholder groups. These key issues were discussed in individual workshop sessions and the findings and views of the workshop were recorded and this report presents a summary and analyses of these findings and views.

The objectives of the study were to establish the current background position of the existing LAWDCs and their WDAs, to identify what alternative roles may exist for LAWDCs, how the issue of value for money may be compared between a LAWDC and a private sector commercial waste operator and whether the involvement of LAWDCs in municipal waste management procurement may create additional capacity/competition in the waste management market.

Key Findings

The key findings of this research are as follows:

- There are considerable variations in the current services provided by the LAWDCs and therefore in the potential for LAWDCs to take part in future procurement bids. The greater the strength of the business and diversity of a LAWDCs operations then the greater potential for future involvement.
- The barriers for the involvement of a LAWDC in a PFI procurement process for an integrated waste management contract appear to be too great to realistically allow a LAWDC to bid as a main contractor. It does not appear that a LAWDC acting as a main contractor can truly meet the current requirements for risk transfer within the PFI process.
- The potential for the involvement of a LAWDC in a PPP procurement process is greater than that for PFI, with more options available for risk management and transfer.

- Disaggregation under PFI or PPP of integrated waste management contracts into smaller self contained elements may result in a risk profile that is more appropriate for a LAWDC to manage and may increase competition. It may also be appropriate for prudential borrowing to be considered for certain contracts.
- Acting in a partnership or joint venture is a clear option for LAWDC to take part in a PFI procurement process, subject to a satisfactory position on risk transfer being reached.
- The potential for the involvement of a LAWDC in a PPP procurement process is greater than that for PFI, with more options available for risk management and transfer.
- Due to the length and complexity of the PFI procurement process, plus the time it can take to construct and commission new technology waste management infrastructure, LAs may require suitable interim solutions to allow short and medium term targets to be met. This is an area where appropriately resourced LAWDCs may be able to competitively bid and increase procurement competition. There may also be opportunities during the interim phase for LAWDCs to act as an interface between Waste Collection Authorities (WCAs) and WDAs to assist in meeting targets.
- There is no consensus on whether the involvement of LAWDCs may attract new entrants and increase competition for municipal waste management contracts; however the converse may actually be the case, the potential for this being solely due to local circumstances.
- A new entrant may prefer to work with a LAWDC in a joint venture, however this may adversely affect the interest of other bidders in the project.
- Sub-contracting is only a workable option if the risks can be adequately allocated and the LAWDC also has a substantial commercial business – it should be noted that LAWDCs are already managing commercial risks under their current operations and that they are able to accept and manage risks where the required services and risk profile match the capabilities and financial strength of the LAWDC.
- It is unclear what the position may be concerning the potential for the creation of local monopolies – views have been expressed that a monopoly created by a successful LAWDC would be a more “benign” monopoly than one that may be created were a LAWDC to be transferred to a PFI contractor, in that the owner of the LAWDC (the WDA) would be less inclined to exploit it’s monopoly position to ensure increased financial returns at the potential expense of the local community (both social and business).
- A key concern of LAs is the loss of value if the LAWDC is allowed to bid but does not succeed in gaining the contract.

CONTENTS

Page

1. INTRODUCTION

1.1 Document Status

This document presents the findings of the Review of Local Authority Waste Disposal Companies and their Role in Future Procurement Project, which has been prepared by Jacobs Babtie on behalf of the Department for Environment, Food and Rural Affairs (Defra)

1.2 Study Objectives

Local Authority Waste Disposal Companies (LAWDCs) were a product of the requirements of Section 32 of the Environment Protection Act 1990. This Section required Waste Disposal Authorities (WDAs) to divest themselves of any in-house provision of waste management services and many WDAs chose to create LAWDCs, operating as "arms-length" companies that generate their own revenues, wholly or partly owned by the WDA.[1]

Many LAWDCs have now been sold off to private sector waste management companies, usually as part of the procurement process for managing the municipal waste of the WDA. Nine LAWDCs now remain in England and Defra has identified that, for five of these LAWDCs, the parent WDAs are undertaking, or preparing to undertake, long-term PFI procurements for the management of their municipal waste and two others are undertaking PPP procurements for such services.

Defra considers that there are capacity constraints upon the UK waste industry and that there are only eight waste management companies that can realistically bid for large, long-term contracts under the PFI or PPP procurement processes. This lack of capacity is already manifesting in limited competition for some WDA contracts and it is considered that this situation will become more acute. Defra have identified that LAWDCs, as they are effectively acting as an existing contractor, are being excluded from the procurement strategy process (and therefore, in effect, the bidding process) and are instead being prepared for disposal.

Defra is of the opinion that the current situation, as outlined above, could result in the loss of LAWDCs as potential additional players in the (already limited) UK waste management market. Defra is also aware of the concern of LAWDCs that they are being excluded from discussions and decisions that can affect their own future.

In order to investigate what roles, if any, LAWDCs may have in future procurement options, Jacobs Babtie (JB) have been commissioned by Defra to carry out an independent review of the remaining LAWDCs and identify what roles they might play in the future procurement by WDAs of municipal waste contracts, including an assessment of the advantages and disadvantages of each role.

[1] It should be noted that Section 32 of the Environmental Protection Act 1990 has been repealed in October 2005 by the provisions of Section 47 of the Clean Neighbourhoods and Environment Act 2005. The potential implications of this change include the ability of Local Authorities to bring back in-house part or all of their waste disposal function. Further details on this matter can be found in the Defra document "Clean Neighbourhoods and Environment Act 2005 – Interim Guidance for Measures commenced on 18 October 2005 (http://www.Defra.gov.uk/environment/localenv/legbill/051018-interim-guidance.pdf).

2. METHODOLOGY

The core information for the study was obtained by conducting 29 structured interviews with relevant stakeholders from the following stakeholder groups:

- LAWDCs
- WDAs
- Financing Bodies
- Financial Advisors
- Legal Advisors
- Others (including HM Treasury, Environmental Services Association)

A list of all the invitees to take part in the study and of all those who did take part is included within Appendix 1 to this report.

Following from an initial meeting with Defra, an interview pro-forma was developed and a copy sent to each invitee who agreed to take part, along with a letter from Defra explaining the purpose of the project. Interviews were conducted face to face wherever possible, with others being undertaken by telephone where necessary.

The interviews gathered relevant information concerning each LAWDC and WDA (where relevant to each interviewee) and sought the opinions of the interviewee on a range of issues relevant to LAWDCs and procurement, e.g. potential roles for LAWDCs, financial issues, legal issues.

The findings of all the interviews were collated and analysed and an interim report on the findings of this analysis was prepared and presented to Defra[2]. This report summarised the responses to the interview pro-forma for each stakeholder group, identified key issues that needed to be addressed in order to establish what roles LAWDCs may have in future procurement, what benefits there may be in these roles and what barriers are present to prevent these roles being realised.

The key issues identified in the report were:

1. The eligibility of LAWDCs to bid for PFI/other procurement methods.

    i. It was clear that there is some uncertainty over whether LAWDCS can bid for PFI contracts. Some interviewees considered that they are ineligible whilst others believed that issues such as transparency, risk transfer and funding can be resolved. Other procurement methods, such as PPP, do not appear to present significant potential barriers to LAWDC involvement.

2. LAWDC financing.

    i. There are a range of opinions concerning the ability of LAWDCs to raise finance and the potential impact that this can have on the parent Local Authority (LA).

[2] Review of Local Authority Waste Disposal Companies and Their Role in Future Procurement, Jacobs Babtie, August 2005

3. Fairness/level playing fields.

   It was clear that there are significant concerns regarding the fairness of competition in a bidding process that includes a LAWDC; however some interviewees have identified mechanisms by which these concerns may be met.

4. Risk transfer.

   One of the main areas of concern expressed by many interviewees is the ability for the LA to adequately transfer risk without it eventually falling back to the LA as the shareholder of the LAWDC.

5. Contract types.

   Waste management procurement does not have to involve a single contract for an integrated service. Disaggregation of the waste management contract may provide greater competition and potential benefits for the WDA. Some interviewees considered that LAWDCs may be in a better position to win such disaggregated contracts.

6. Value for money.

   The issue of how to assess the value for money of a LAWDC (or a private waste management contractor) was unclear, with a number of interviewees considering that socio/economic issues should also be considered as well as “bottom line” costs for service. The potential for dividends from the LAWDC should also be considered.

7. LAWDCs providing services to non-parent Local Authorities.

   Some LAWDCS are already providing some waste management services to non-parent LAs. The potential of a LAWDC providing an integrated waste management service to another LA raises issues including risk transfer – the parent LA will have consider whether it wishes, as the whole/majority shareholder of the LAWDC, to assume the potential risk of the LAWDC failing to achieve another LA’s targets.

8. Competition

   LAs are concerned about getting adequate competition for their waste management contracts (e.g. in Northumberland there was only one bidder for the contract). Various views were expressed as to whether the presence of a LAWDC would increase competition or not. This is a very subjective issue and one that WDAs would find difficult to test.

9. Ability of LAWDCs to deliver integrated waste services.

   It was recognised that there is a wide range in the services provided by different LAWDCs and that not all would be able to deliver an integrated waste service.

A workshop session was then held at the Jacobs Babtie offices in Birmingham, where these key issues could be debated and, if possible, resolved by discussions amongst representatives of the stakeholder groups. Suitable representatives from the stakeholder groups were invited to attend and representatives from the following companies/Local Authorities agreed to attend the workshop:

- Defra
- Cumbria County Council
- Yorwaste

- KPMG
- Inglefield Capital
- NIP Capital

In order to address the key issues highlighted in the interim report, the following workshop sessions were held:

A. The scope for LAWDCs.

To consider and attempt to reach consensus on what scope a LAWDC may have to take part in procurement for integrated waste services, for example their legal powers, ability to provide required services, ability to raise finance.

B. Value for money.

To consider what issues should be considered in the context of the value for money of a LAWDC and how such a measure could be made.

C. The value of LAWDC involvement in procurement.

To consider what benefits there are in LAWDCs taking part in the procurement process, including potential future roles for LAWDCs.

D. Barriers to LAWDC involvement.

To consider what barriers exist to prevent LAWDCs being involved in procurement and what options are available to overcome these barriers.

E. Risk transfer.

To consider how risk transfer can be achieved in the available procurement options and how a LAWDC may transfer risk.

The outcomes of the workshop were collated and analysed and the findings are presented in Section 4 of this report.

3. CURRENT LAWDC OPERATIONS

3.1 Introduction

At the time this study was carried out, there were nine remaining LAWDCs in England. These were:

- County Environmental Services (WDA Cornwall County Council)
- Coventry and Solihull Waste Disposal Company (WDA Coventry City Council and Solihull Metropolitan Borough Council)
- Cumbria Waste Management (WDA Cumbria County Council)
- Greater Manchester Waste Group (WDA Greater Manchester)
- Mersey Waste Holdings (WDA Merseyside)
- Norfolk Environmental Waste Services (WDA Norfolk County Council)
- Premier Waste Management (WDA Durham County Council and Darlington Borough Council)
- Wyvern Waste Services (WDA Somerset County Council)
- Yorwaste (WDA North Yorkshire County Council and City of York Council)

The following paragraphs provide a summary of the operations for each of the above LAWDCs, along with other key information such as current procurement status of the WDA (based upon information provided by each LAWDC/WDA).

3.2 County Environmental Services

County Environmental Services (CES) operate facilities within Cornwall and provide service contracts in Cornwall and West Devon. The company articles do not restrict their area of operation. CES provide landfill and transfer station/civic amenity site services and state that they own the following assets:

- 2 operational landfills
- 4 closed landfills
- I transfer station (TS).

CES also own a subsidiary company and have a total of 140 staff.

CES have a contract with Cornwall County Council to provide landfill services to 2013; however it is understood that this contract may be terminated early due to the current PFI procurement process being undertaken by the Council. CES were also contracted to the Council to provide civic amenity site services but this contract has recently expired.

CES have several commercial and industrial contracts and currently manage approximately 250,000 tonnes per annum (tpa) for Cornwall CC and a further 100,000 tpa for various commercial/industrial customers. Turnover is approximately £17M, with approximately 50% of turnover from the Council contracts.

The Council are currently undertaking a PFI procurement process for an integrated waste management contract. Bidders for the contract were given the following options in relation to CES:

i. Transfer of shares to bidder

ii. Transfer of assets to bidder

iii. Sub-contract for landfill services provided by LAWDC to bidder.

All bidders at ITN proposed option (ii), with a reduction in gate fee for the value of the assets transferred rather than a capital receipt for the Council.

The Council consider that the LAWDC could not tender for the PFI contract as there would be insufficient risk transfer to satisfy SOPC3, nor would the LAWDC be able to satisfy the pre-qualification requirements.

3.3 Coventry and Solihull Waste Disposal Company

Coventry and Solihull Waste Disposal Company (C&S Waste) operate facilities in Coventry for Coventry and Solihull WDAs. They also currently take waste from Warwickshire and Hereford and Worcester (20,000 tpa).

C&S Waste own an energy from waste plant and a civic amenity (CA) site, plus one closed landfill site. They employ 69 full-time staff.

C&S Waste is currently operating on an extension to the waste contract with Coventry and Solihull Councils. This provides 190,000 tpa of waste and the energy from waste plant has a maximum capacity of 220,000 tpa $\pm$ 5%. The capacity to tender for other waste streams is therefore limited. Turnover is approximately £10M per annum and they have experienced no problems in obtaining commercial loans, with £20M investment raised through the banks.

Coventry City Council (CCC) has submitted a PFI outline business case which C&S Waste now believes will be withdrawn. Robs & Rose advised for PFI initially from reviewing the sale of C&S Waste. The PFI case has stagnated now as targets are met for recycling. C&S Waste believes that the Council appears to like the LAWDC principle. C&S Waste considers that they could not bid for a PFI contract and that a partnership with a waste management company may have too many conflicts of interest.

3.4 Cumbria Waste Management

Cumbria Waste Management (CWM) operates facilities within Cumbria, excluding South Lakes, for Cumbria County Council.

CWM operate 3 active landfills, one of which is a joint venture, that are leased from the Council/joint venture. They also operate CA sites and provide a green waste collection and composting service. CWM owns some plant (including vehicles and a leachate treatment plant), operates a commercial hazardous waste transfer station and is commissioning a liquid waste treatment plant. CWM employs over 100 staff.

CWM manages approximately 220,000 tpa, of which approximately 190,000 tonnes is landfilled. Turnover is just over £12M.

Cumbria CC are currently tendering for an integrated waste management contract via PPP. The Council intends to sell the LAWDC, however they have recently introduced a mandatory variant to the bid to provide an option for CWM to remain as the landfill provider. CWM consider that they could have entered into the bidding process but for the pre-qualification turnover requirement – and that this could have been resolved with a suitable partnership/consortium approach. The Council consider that if the procurement process was starting now then they would probably try to include CWM in the process; however they consider that the process is now too far advanced to change.

3.5 Greater Manchester Waste Group

Greater Manchester Waste Group (GMW) operates facilities within Greater Manchester (excluding Wigan). They provide domestic and commercial waste collection, recovery, recycling and disposal services. They also operate an energy from waste plant and provide waste management training and consultancy services. GMW do not own or operate any landfills and use commercial landfills for the disposal of waste (other than via the energy from waste plant).

GMW own the real estate or leasehold for all plants except the energy from waste plant and employ approximately 1000 staff. They manage 1.2 – 1.4 M tpa of waste from the WDA and state that they have a turnover of approximately £100M.

The current WDA contract expires in April 2006 and the WDA have a well-advanced PFI procurement process for an integrated waste management contract. The WDA consider that disposal of GMW is likely to be the best value option and they do not believe that a LAWDC could satisfy the risk transfer requirements for a PFI contract. The WDA undertook an exercise to asses the ability of GMW to pre-qualify for the PFI tender and consider that they would almost certainly have failed on grounds of turnover, ability to raise project finance, and a lack of suitable track record for making planning applications, waste management licence applications and PPC permit applications.

3.6 Mersey Waste Holdings

Mersey Waste Holdings (MWH) operate facilities in Merseyside, Halton and Warrington. They provide disposal, management of household waste recycling sites (HWRC), waste collection, monitoring and technical consultancy services. As part of a joint venture they will also soon be operating a landfill in North Wales.

MWH own land assets and part-own a landfill site. They employ approximately 250 staff and manage approximately 950,000 tpa. The forthcoming opening of a TS, HWRC and in-vessel composting facility on the Wirral will boost tonnages by at least 100K tpa. The Group has a turnover of £40M.

MWH have a disposal contract with the WDA until 2008. The WDA have just appointed advisors to assist in the procurement process. So far, the advice they have received is to undertake a share sale of the LAWDC with the contract. The WDA is not adverse to MWH being involved in the procurement; however it does have concerns over issues of risk transfer and level playing field.

3.7 Norfolk Environmental Waste Services

Norfolk Environmental Waste Services (NEWS) operate facilities within Norfolk, currently managing 11 CA sites, operating three TS, two landfill sites (plus one mothballed), one materials recovery facility (MRF), a composting facility, commercial waste collection and waste broking with a firm that deals with hazardous waste.

NEWS own the land and buildings for one MRF and one CA site. They also own three closed landfill sites. They employ 70 directly employed staff and manage approximately 205,000 tpa. NEWS have a turnover of £11 - £12M.

NEWS have a disposal contract with Norfolk County Council (NCC) and management of recyclables contracts with local District Councils. NCC are in the process of letting a 25 year PFI contract (without credits) for residual waste treatment (to be awarded in March 2006) and NEWS have passed the pre-qualification, submitted a bid and are now one of two remaining bidders. The Special Purpose Vehicle (SPV) is formed of NEWS, Lloyds Bank and Innisfree and the bid has been undertaken with project finance and NCC's advisers are satisfied over issues of vires and state aid. The bank requires two contracts – one with a construction contractor to design and build a new technology plant (anaerobic digestion), with the construction contractor assuming the technology risk and a contract with NEWS to run the facility (including lifecycle management). The bank were informed that no parental guarantees were possible and so they have a step-in clause for poor performance. The SPV itself has very limited risk and the bank considers that NEWS are able to manage their risks and also any potential penalties. Some risk management/transfer issues are still to be determined (e.g. planning risk). NCC is also preparing a PFI tender for 2010 onwards, to be awarded in March 2008. NEWS could possibly bid for this.

3.8 Premier Waste Management

Premier Waste Management provide waste management services in NE England, Northumberland, Durham, Tyne& Wear and Teesside. They provide landfill, treatment (aerobic digester), TS and HWRC, aggregates recycling, as well as commercial and trade waste collection services.

Premier Waste Management own and operate 2 landfills, an aerobic digester and a depot. They employ approximately 320 staff and manage approximately 1M tpa, with a turnover of £38M in 2005. Premier Waste Management state that they operate the largest collection service in the NE and have possibly the largest landfill void in the NE. They also have the rights to manufacture and sell the aerobic plant technology that they use in NE of England.

They have contracts with Durham CC, Darlington DC and South Tyneside for disposal services and TS/HWRC management, along with kerbside recyclates collection and transfer services for Gateshead and Sunderland and green waste composting for all the above authorities. They also have a wide range of commercial contracts for collection, disposal and treatment services.

Durham WDA considers that future procurement is not likely to be PFI at this stage. They are pleased that Defra are looking at a potential role for LAWDCs and consider that Premier Waste is well managed and is at the forefront of technology development. They consider that the retention of Premier Waste and its expertise could well benefit Durham CC.

3.9 Wyvern Waste

Wyvern Waste provides waste management services principally in Somerset and Bath, with some operations in Bedfordshire and Oxford. They provide landfill, HWRC and collection services, with some composting and recycling.

Wyvern Waste own 5 landfill sites – 2 core sites with over 12 years capacity, 4 HWRC sites under management, 2 TS (plus 1 in “hibernation”), 1 MRF, 3 windrow compost sites and one in-vessel composting plant. They employ 180 staff and manage approximately 450,000 tpa for landfill and 40,000 tpa for composting, with a turnover of £23.9M for 2004/05.

The core contract with Somerset County Council is until 2007 with an option for an additional two years, the contract with Bedfordshire is until 2007 with option to extend to 2012 and the contract with Bath and North East Somerset (BANES) until 2007.

Wyvern Waste is currently in the process of being sold by Somerset County Council to a preferred bidder under a PPP procurement. Tender returns are due for 30th September 2005 with sale anticipated, subject to SCC Scrutiny panel review, by the end of the current financial year.

The WDA state that the PPP contract has been drafted to be SOPC3 compliant in the eventuality that PFI may occur down the line.

3.10 Yorwaste

Yorwaste provide facilities within North Yorkshire and City of York and services customers in North, West and South Yorkshire. They provide landfill, bulking and transport of recyclables, composting, liquid waste treatment, MRF, commercial and kerbside waste collection and HWRC Management services.

Yorwaste do not own any landfills but have six landfills on long-term leases. They operate three MRF/bulking operations, four composting sites, one waste transfer and recycling centre, one transport depot and one liquid waste treatment plant. They employ 140 staff and manage approximately 1M tpa, with a turnover of approximately £17M in 2004/05. The business is split 50/50 shareholder/commercial.

Yorwaste have landfill contracts with North Yorkshire County Council (NYCC), City of York Council (CYC), Bradford City Council and Leeds City Council. They also provide composting services to NYCC, CYC, Leeds City Council, Scarborough, Wakefield, Hambleton and Richmondshire. The contract durations vary from 2007 – 2015 for CYC and NYCC.

Yorwaste have recently successfully tendered for the NYCC landfill and composting contract to 2015, with elements of the tender being similar to PFI/PPP.

3.11 Summary

A table summarising the information provided for the LAWDCs is provided as Appendix 2 to this report.

4. WORKSHOP OUTCOMES

4.1 Introduction

As detailed in Section 2 of this report, the following five workshop sessions were held to consider the key issues identified by the stakeholder groups:

A. The scope for LAWDCs.

B. Value for money.

C. The value of LAWDC involvement in procurement.

D. Barriers to LAWDC involvement.

E. Risk transfer.

Following a review of the options available for LAWDCs in procurement, the outcomes from each session are detailed in Sections 4.3 to 4.7 below. The information presented in these Sections reports the discussions within the workshop sessions and does not necessarily represent the opinions of Jacobs Babtie and/or Defra.

4.2 Options for LAWDCs

A table summarising the options for LAWDCs to be involved in PFI procurement, together with an assessment of the potential pros and cons of each option and an analysis of how the LAWDC may proceed under each option, is provided overleaf. The assessment is based on the perspective of a LA as the final decision maker on the future of a LAWDC. Whether the identified pros/cons are relevant to a LA will depend upon the performance of the particular LAWDC and the views of the LA concerning the LAWDC, as well as the nature of the tender (duration, extent etc).

Table 1. LAWDC options

Option 1 – LAWDC as main contractor	
Pros	• Retention of LAWDC. • Retention of perceived "control" over waste management. • Maintenance of WDA/LAWDC relationship (if good). • Increase in shareholder value. • Payment of dividends. • Could prevent the formation of a regional monopoly. • Ease of transition.
Cons	• Loss of potential sale revenues. • Maintenance of WDA/LAWDC relationship (if poor). • Lack of risk transfer from WDA. • Formation of regional monopoly (if LAWDC is sole provider of services in the region).
How may a LAWDC undertake this option?	The particular balance of pros and cons will depend on the WDAs view of the LAWDC, including performance, value for money and the political views of the WDA concerning LAWDCs. The lack ability to fully transfer risk to a LAWDC is a main concern for WDAs and can only really be addressed by a reconsideration of Government and LA requirements for risk transfer in PFI procurement – perhaps to identify which risks are acceptable/manageable and which must be transferred. The ability for a LAWDC to undertake the role of main contractor in a PFI procurement process appears to be prevented by the requirement for risk transfer from the WDA. This issue may be resolvable through the use of risk transfer mechanisms by the LAWDC to its subcontractors.
Option 2 – LAWDC in joint venture/partnership	
Pros	As for option 1 above, plus: • Access to skills/technologies/finance from partners. • Greater potential for risk transfer.
Cons	As for option 1 above, plus • Additional resource required to set up and manage the joint venture/partnership. • The legal position is such that the LAWDC may be effectively seen as being the LA., and therefore it is the LA that is within the partnership/joint venture. This may cause complications with issues such as State Aid and competition law, however these issues may have been satisfactorily addressed by NEWS in its bid for a treatment contract in Norfolk.
How may a LAWDC undertake this option?	The ability for a LAWDC to act as part of a joint venture/partnership will clearly depend upon the choice of partners and the ability of the joint venture/partnership to provide suitable funding, facilities and risk transfer. The particular balance of pros and cons will depend on the make-up of the joint venture/partnership and the ability of it to deliver the required waste management services. The potential for greater risk transfer from the WDA is a significant issue, as is the potential access to funding for the LAWDC.

Table 1 – LAWDC options (continued)

Option 3 – LAWDC as subcontractor	
Pros	• Retention of LAWDC. • Retention of some perceived "control" over waste management. • Potential for payment of dividends. • Risk transfer from the WDA increased. • Access to skills/technologies/finance from the market.
Cons	• "Attractiveness" of LAWDC to main contractor. • Potential loss of shareholder value. The LA would need to be satisfied, as far as it is able to, that the business is commercially sustainable in the long term.
How may a LAWDC undertake this option?	This is an option that has been offered to bidders in a number of procurement exercises but does not appear to have been taken up by any bidders. The attractiveness of the LAWDC as a subcontractor will depend upon the value of its assets and the services it can offer, however if its assets are considered of value then a bidder is likely to prefer to acquire the assets. This is not an option likely to be driven by the LAWDC, but may be an option that the WDA decides to offer in the tender. It's attractiveness as an option could be dependent upon local circumstances.

For PPP procurement, the main issues remain as in Table 2 above, however there are some significant differences:

- The WDA has more discretion in terms of risk transfer.

- The WDA could raise finance for the LAWDC, possibly via the prudential borrowing route.

- The procurement would not be driven by the need for PFI credits, so an incremental approach could be followed (it should be noted that the issue of PFI credits is not a true restriction within PFI procurement but it is perceived as an influence).

4.3 The Scope for LAWDCs

This session considered what scope a LAWDC may have within waste management procurement. The following main points were raised:

- LAWDCs currently provide general services such as landfill and civic amenity sites, with some LAWDCs already providing new technology waste treatment and recovery solutions. To provide technology such as mechanical biological treatment (MBT) and energy from waste, for most LAWDCs this would probably need to be acquired through some form of partnering. It is understood that there is a lack of expertise in certain areas but there is no reason why a LAWDC cannot buy in that requirement. It is also recognised that many private waste management companies lack expertise in similar areas, e.g. operation of MBT and energy from waste plants.

- It was considered that it would be useful to compile a more comprehensive list of LAWDCs detailing their facilities (assets held) e.g. landfills, civic amenity sites, technology. This information could be used to highlight the potential of each LAWDC to deliver the set waste requirements of that area. This would in turn allow the funding organisation etc to determine where investment would be best placed. It is the view of the workshop that not all LAWDCs provide services other than landfill and civic amenity sites.

- LAWDCs have investigated the marketplace to determine the different types of available technology. The extent of these investigations have been variable, with some LAWDCs already providing new technology solutions and others having explored the various options in order to obtain these services if required to by the WDA.

- LAWDCs believe that LAs should be considering interim solutions now, to ensure that infrastructure is quickly developed to save the penalties that will be incurred as a result of failure to meet regulatory requirements. This can be delivered via the LAWDC providing treatment technologies etc, which may also be a benefit to the shareholders. The workshop considered that this was a significant role that the LAWDCs could play, especially as some PFIs will not be complete until 2007-9 and the impact on diversion may not be seen until after 2010-12.

When considering whether an individual LAWDC could realistically bid for a PFI, the workshop identified the following key points:

- There would need to be a detailed assessment of their experience, expertise and involvement in risk transfer.
- The banks are very likely to require guarantees from a parent company to cover the risk/liabilities and the LA would be unwilling to provide such a guarantee to the LAWDC due to conflict of interest.
- Without a parent company guarantee, the LAWDC may seek a joint venture (JV) with another party to take on the risk.
- There would need to be a consideration of the existing assets that the LAWDC currently holds and an assessment of those assets against the requirements of the PFI.
- Lenders will require security over these existing assets as a condition of their financing. LAs and LAWDCs may have difficulty in effectively putting the ownership of these assets at risk.

Prudential borrowing is available to LAWDCs and LAs are able to lend directly into a LAWDC from the shareholder authority, however the LAWDC is part of the consolidated accounts of the LA. The LAWDC can therefore only borrow funding if it can repay the debt of the unsupported borrowing. Payback on borrowing can be measured for waste schemes via waste modelling and investment now can be used to offset penalties such as LATS.

In conclusion, the scope for LAWDCs appears limited, with the following issues being apparent:

I. LAWDCs need to acquire relevant skills e.g. partnering to provide full range of services.
II. A funding appraisal for the LAWDC will be required to assess its level of borrowing potential.
III. LAWDCs must undertake an in-depth market research on suitable technologies to identify robust solutions.
IV. If there is disaggregation of contracts then a JV could use corporate finance rather than project finance to fund infrastructure projects such as MRFs and/or CAs.

4.4 Value for Money

This session debated what issues should be considered when determining the value for money of a LAWDC and how such issues could be measured. The following main points were raised:

- LAWDCs believe that they can provide a service via their long-term experience and relationship with the local community that offers value for money. The LAWDCs can also have a track record in obtaining planning permission for facilities within their geographic area, which may give them some advantage when understanding the environment in which they operate. The difficulty for the LAWDCs is that these factors are not tangible and cannot be quantified but they do consider that an element of trust exists within the community that would help the LAWDC deliver the pathway that the LAs wish to follow and therefore assist in providing value for money.

- LAWDCs consider that if a main commercial waste operator acquires the LAWDC through a contracting process, this may achieve a monopoly in that geographic area. Increased pricing maybe a result of that monopoly and therefore reduce the value for money delivered by the operator. It was also considered that such a monopoly would also have a “knock-on” effect in raising waste management prices for local commercial and industrial waste producers, thus impacting on the local economy as a whole. The presence of the LAWDC may therefore prevent such a monopoly and so assist in providing value for money, however there is also the potential for a monopoly to be created by the LAWDC – this would reduce competition and potentially result in reduced value for money. The potential for the LAWDC to exploit its monopoly is less than a private sector player as a LAWDC has a shareholder that is responsible for the community as a whole, including the business community.

- Commercial waste operators are constrained by the requirement for a commercial rate of return. LAWDCs are not constrained by this; therefore this would give them greater flexibility in pricing. There is also the potential for the LAWDC to offer a dividend its LA.

In conclusion, when considering what constitutes value for money the LA will have to take into account the ability of a LAWDC to satisfy the following key issues:

I. Price.
II. Quality of service.
III. Customer satisfaction.
IV. Socio economic values.
V. Deliverability.

It should be noted that, whilst these were the views of the workshop on how a LAWDC can provide value for money, in the initial interviews some of the WDAs expressed doubts that their LAWDCs were truly providing value for money, whilst accepting that it was a difficult issue to measure.

4.5 The Value of LAWDC Involvement in Procurement

This session considered what benefits might be gained by involving LAWDCs in the procurement process, including what roles a LAWDC may play. This was achieved by firstly agreeing on key problems currently experienced in waste procurement, then looking at ways that LAWDCs might contribute to solving these problems. The following conclusions were reached:

- Initially, the following problems were identified with current waste procurement in general, and particularly the PFI process:

  - The availability of suitable sites.
  - Obtaining planning permissions – this can be a complex and very time consuming process, often with no guarantee of success.
  - The maturity of the Sector – the “waste disposal technology” sector is considered to be relatively immature by financing bodies, and financier confidence is low. This reduces availability of debt and increases the cost of financing overall, potentially to an unacceptable level.
  - Technology risk remains an issue in many cases.
  - Commercial balance sheet strength / capacity in the private sector – it is considered that there is insufficient financial strength to finance all the waste treatment/disposal assets that may be required in England and that the private sector may already be overstretched.
  - Challenging LATS targets both increase and complicate the issue of private sector capacity.
  - Regional market strength – there is potential for regional monopolies to develop, affording companies undue pricing power in the locality.
- The procurement process overall is complex and expensive

It was noted that many of these concerns relate mainly to the disposal and /or treatment of waste, rather than its collection.

It was then considered how LAWDCs might add value to procurement. The following possibilities were identified:

- Benchmarking – comparing a private bidder’s pricing to the audited LAWDC solution.

- LAWDC participation as part of a disaggregated contract procurement, thus promoting a "mixed economy" of waste suppliers. This should diversify supply and therefore reduce some risks, as well as promoting continuing competition between suppliers.
- Collection & recycling can provide a "quick win" for meeting LA targets. In addition, these less capital intensive areas often lend themselves to a prudential borrowing solution, making it easier for LAWDCs to be involved.
- The LAWDC might act as an asset owner, e.g. retaining the key landfill sites in an area, making the playing field more level for other bidders for a contract.
- LAWDCs may enter into partnership with entities other than major incumbents, thus widening the number of players involved in the waste management field and increasing competition. However, concern was noted that that the involvement of a LAWDC risks "frightening off" other bidders in a competitive process
- Inclusion of the voluntary sector – the LAWDCs may be well placed, as a local organisation, to work with voluntary organisations involved with recycling in the area. This could also assist in the development of recyclate markets.
- LAWDCs can currently act as an interface between waste collection authorities (WCAs) and the WDA. In a disaggregated contract scenario, this role could be continued and expanded to include acting as the interface between different contracts and undertaking a project/contract manager role.
- Other markets can be a growth area for LAWDCs, for example commercial waste collection and disposal services and other local "niche" markets.
- The commercial waste sector has good potential for LAWDCs – many are already very active in this sector and derive significant revenues from it.

4.6 Barriers to LAWDC Involvement

This session considered what barriers exist to a LAWDCs' involvement in procurement. The following conclusions were reached:

- It was identified that when bidding in a procurement process, a LAWDC broadly has the following three options:

  - Main contractor
  - Partnership/Joint Venture (JV)
  - Subcontractor (where no prescribed subcontractor arrangements exist, the LAWDC can continue to provide specific parts of the waste service).

- For involvement in waste procurement, the following barriers are present:

  - Bid costs in PFI are very high – the private sector is more experienced in controlling a PFI bid process and can afford to hire suites of advisers to tackle this issue.
  - Pre-qualification hurdles – LAs may set financial and technical requirements in a PFI bid that are too high for LAWDCs, e.g. track record, size, financial strength.
  - The availability of PFI credits may encourage a LA to undertake a PFI procurement process when other procurement mechanisms may be a better option overall for the waste disposal service and may also allow the LAWDC to take part.
  - In PFI contracts, the severity of payment mechanisms for failure to meet targets can be disproportionate to the financial strength of a LAWDC, unless these can be proportioned within a partnership/JV structure.
  - If a LAWDC is in partnership with a private sector entity for a PPP procurement, this creates complexity over access to prudential borrowing for the JV – the availability of the borrowing to the private sector partner causes difficulties in the area of procurement and public subsidy. In addition, the LA would be risking its own money in an entity over which it does not have full control.
  - Risk capacity of the WDA shareholder – unless the LAWDC is in some form of JV in which the risk is transferred to the private sector part of the JV, then the final risk lies with the shareholder – the parent WDA. Risk is therefore not transferred away from the LA. There needs to be a detailed consideration of the implications of this issue, i.e. is risk

being borne by the party best placed to manage it and is the degree of risk retained by the LA substantially different from the position with a private waste management company?
- Should the LAWDC bid but not win the contract, the remaining company may not be financially viable and there will therefore be loss of shareholder value.
- The shareholder role that the WDA has is of interest. Are WDAs being proactive as shareholders – how well positioned / skilled is the WDA to be an effective shareholder, maximising efficiency and profitability of the LAWDC?
- Some advisors may consider that LAWDCs do not have the ability to manage contracts with high levels of project finance, however it should be noted that some private sector waste management companies also have limited experience of project finance.
- There is a perception that the weighting of evaluations under procurement processes may be biased towards commercial waste operators. LAs and their advisors should ensure that assessment and weighting scores do provide an equal assessment
- The Treasury options model always appears to come up with PFI as the solution – it appears to have an in-built assumption on public sector efficiency which may not truly match reality.

- Which roles are available or suitable for LAWDCs to take will depend upon the procurement option being followed. It is clear that the PFI process does not easily lend itself to the involvement of a LAWDC in a way that allows the LAWDC to remain as an arms-length company wholly owned by a LA, whereas a PPP process would appear to allow a LAWDC to consider a range of options for involvement.
- LAs need to be certain that they have conducted a robust assessment of alternative procurement options in order to ensure that the chosen option is the best option for the LA.

4.7 Risk Transfer

It has already been identified that the issue of risk transfer is one of the key barriers for LAWDCs taking part in a PFI procurement process. This workshop session considered how a LAWDC might manage the risk transfer requirements of the available procurement options and the following conclusions were reached:

- LAWDCs posses little experience of risk management in PFI, however it should be noted that until relatively recently the same was also true for the private sector waste management companies.
- The technology provider often needs to have a parent guarantee to ‘wrap’ the company, as they tend to be a small design and build specialist. Therefore the ‘wrap’ company that acts as the parent service provider tends to be a major waste operator such as Shanks, SITA, Biffa, Onyx etc.
- The Financial Advisers perspective is that there needs to be a clear understanding of the level of risk by the LA, operator and lender, before the PFI route is taken.
- Under PFI, when a performance target is not achieved the financial penalties can be severe and can critically impact upon the operator, therefore the operator must be completely confident that the technology can be provided on time and the performance delivered. This can only be identified by a track record of experience.

The session concluded that a potential mechanism for managing risk transfer and enabling LAWDCs to take part in the procurement process is to break contracts down into suitably self-contained individual elements (disaggregate), and for the LAWDCs to bid for those individual requirements. As the contracts and pursuant risks are smaller, the LAWDCs are more able take on these risks. These contracts could have a shorter term of agreement, e.g. 5 years, compared with a PFI. The PPP procurement process appeared to be the best way to pursue this approach. The workshop also concluded that this may increase the level of competition available for the procurement process and that its increased flexibility may be of more benefit in the long term than a fixed, integrated 25 year contract. The workshop recognised that a number of disaggregated contracts would require more contract management by the LA than a single integrated contract.

5. ANALYSIS OF OPTIONS

5.1 Introduction

This part of the report considers what options are available for the involvement of LAWDCs in the different procurement options and provide conclusions concerning the options that LAs may wish to consider when developing procurement strategies.

5.2 PFI Procurement Options

The barriers for the involvement of a LAWDC in a PFI procurement process for an integrated waste management contract appear to be too great to realistically allow a LAWDC to bid as a main contractor. Initially, the pre-qualification requirements for turnover, experience and track record are likely to be too great for most, if not all LAWDCs, to satisfy as a main contractor. Should, however, the pre-qualification requirements be met by a LAWDC, the potential cost of making a PFI bid may be too much for the LAWDC to take the risk of bidding. Finally, it appears likely that a LAWDC acting as a main contractor cannot truly meet the requirement for risk transfer within the PFI process, as it stands, in that the risk eventually passes back to the LA as the shareholder (although there are varied opinions on this point). This would be of particular concern to any LA whose LAWDC may wish to take on a PFI contract for another LA. The following table indicates the potential for risk transfer to a LAWDC, where the LAWDC is the main contractor:

Table 2 – Potential for Risk Transfer to LAWDCs

Risk Type	Risk Description	Degree of Risk Transfer
Performance	Risk of failing to meet contract targets.	This risk would be retained by the LAWDC and hence by default the LA. Effectively the LAWDC would need to define the technical solution, scale of plans etc. The LA would need to decide if the LAWDC (and by default itself) are best placed to manage this risk.
Operating	Risk of increased operating and maintenance costs.	Risk transfer to Operation and Maintenance Contractor - this may be the LAWDC but could be a third party.
Planning	Risk of failing to obtain necessary planning permission by required dates.	This would be retained by the LAWDC, however many LAs are recognising that they may be best placed to manage this risk.
Technology	Risk that the technology does not perform as expected.	Transfer to technology supplier.
End Market	Risk of failing to gain expected incomes from sale of recyclables etc.	This would be retained by the LAWDC. Current PFIs transfer this to the private sector in varying degrees; waste management companies will only accept this risk within defined limits.
Construction	Risk of cost and/or time overruns.	Transfer to construction contractor.

The above table shows that, where the LAWDC is the main contractor, risk transfer will effectively be similar to a traditional procurement. The LA will effectively assume the risk of defining the solution and also be exposed to some market risks, therefore the LA will need to satisfy itself that it is best placed to manage these risks.

Other potential roles available to a LAWDC in a PFI procurement process are as a subcontractor or within a partnership or joint venture.

Acting as a subcontractor has its own risks, as the main contractor would attempt to transfer as much of its risk liabilities as possible onto subcontractors. However, the risk capacity of the LAWDC can be quantified to assess whether the demands of the sub contract arrangement can be met. The level of security for the LAWDC would also be very different compared to its previous role as a main contractor for an LA, e.g. there may be no guarantee that it would maintain the subcontractor role over the lifetime of the main contract. This option may be suitable for LAWDCs who have substantial (and growing) revenues from commercial/industrial waste contracts. This is an option that LAs can consider offering their LAWDC within a PFI procurement process.

Acting in a partnership or joint venture is a possible option for a LAWDC to take part in a PFI procurement process. As has already been noted, one LAWDC (Norfolk Environmental Waste Services) is currently a preferred bidder in a PFI procurement process (without credits). A wide range of possible partners have been identified, from the major waste disposal companies to technology suppliers, financial institutions, construction companies and overseas investors. There is an opportunity for LAWDCs to manage the risk transfer issue of PFI by ensuring that the risk is retained by the other member(s) of the partnership/joint venture (some technology suppliers appear to be offering this option). However this would require very careful consideration as, should the risk holder fail to be able to manage the risk and incur penalties that it cannot meet, the potential remains for the risk to eventually fall back to the LAWDC, with consequences for the value of the LA's shareholding. There is also the risk that any partner will argue or dispute liability, leading to a need for dispute resolution.

The whole issue of risk transfer to a LAWDC is complex. On one level, the LAWDC is a "stand alone" company and if it has appropriate skills and fiscal strength it should be as able to take on and manage risk as any private company. However, as the LA either owns all or a substantial part of the LAWDC, the value of the shareholding cannot be uncoupled from the risks being assumed by the LAWDC.

It has been made clear in this study that financiers and LAs have a strong desire to see clear allocation of risk. Unfortunately, when considering how a LAWDC may take part in a PFI project then this is not the case. We believe it may be possible to resolve these issues but it would take time and require a pioneer authority to test potential resolutions. The progress of NEWS in their current procurement bid should be closely monitored.

There are therefore some obvious difficulties for a LAWDC taking part in a PFI procurement process. We believe that there are two critical conditions that must be met before a LAWDC can take part – these are:

- Demonstration of the ability to provide and finance all required services, either in their own right or within a JV/partnership.
- Ability to satisfactorily demonstrate risk transfer through contract structure or JV/partnership arrangement.

In addition, there are significant concerns over competition in the sector and it is unclear that the involvement of a LAWDC would improve this situation. In the event of limited competition, a LA may need to assess value for money through some form of benchmarking process. The LA will also need to consider the potential impacts of an unsuccessful bid by the LAWDC and satisfy itself that, in such circumstances, the LAWDC will continue to be viable.

In conclusion, there appears to be little room for LAWDCs to take part in PFI procurement in a way that would be of benefit to the LAWDC and its shareholders, given that LAs are very risk averse. Should a LA decide to go down the PFI route then other options, such as sub-contract or transfer of the LAWDC, would appear to be the most likely for the LA. The table below provides an analysis of each option for a LAWDC in a PFI procurement scenario and considers if the option would increase competition, which will be of benefit to the LA in ensuring competitive contract costs, and whether a LAWDC could manage each option:

Table 3 – PFI Procurement Analysis

LAWDC Option	Does it increase competition?	Can the LAWDC manage this option?
Main contractor	If there is a potential for limited competition, then this may be the only way to increase the number of bidders. Private sector contractors may not wish to bid against a LAWDC unless they can be assured that there is a completely level playing field.	Unlikely, due to pre-qualification requirements, bidding costs and risk transfer issues.
Partnership/joint venture	As above for main contractor, plus the inclusion of appropriate partners may result in a greater choice of technology options.	Possibly. NEWS appears to be following this option, however it is not yet known if the methodology adopted will be sufficiently robust to pass the further scrutiny that their bid will now undergo. LAs will still require clarity of risk transfer.
Subcontractor	Could increase competition in a municipal waste PFI procurement, as some technology suppliers may be interested in this option. The retention of the LAWDC may also result in increased competition being available within the commercial waste sector.	Yes, but the indications from the large waste management companies are that the bidder would prefer to acquire the LAWDC assets. This is not necessarily the case for other new entrants.

5.3 PPP Procurement Options

Under this procurement mechanism, there would appear to be greater options for risk management available to the LAWDC – this would assist the LAWDC in the formation of suitable partnerships or joint ventures to meet the requirement for new technology solutions.

One option that was highlighted by a number of interviewees and attendees of the workshop and is available under PPP procurement is to disaggregate the integrated contracts into several smaller contracts (whilst this option is also possible in a PFI procurement, the transaction costs and the desire of the LA to include maximum capital expenditure in order to obtain maximum PFI credits are major disincentives). The potential advantages of this option for LAWDCs is that it would enable them to bid as the main contractor for those areas where they have strengths without having to meet the high level of prequalification required for an integrated bid. It would also allow the formation of joint ventures/partnerships with potentially more options available for risk management (assuming that the risk to be transferred for each contract would be proportionate to the level of risk impact that the contracted operation has). The potential advantage for LAs is that this may result in more bidders (and hence more competition), particularly in those areas such as waste collection and the management/operation of CA sites and MRFs where some smaller local waste management companies may have the experience, finance and facilities required to make a credible bid. Potential disadvantages of this approach for LAs are that the management of several contracts is likely to be more complex than for a single integrated contract and the larger waste management companies who can provide the new waste treatment technologies may find smaller contracts less attractive, although this may also encourage other technology providers who do not want to get involved in running landfills or taking ownership of a LAWDC etc. This may be of benefit for WDAs (competition), LAWDCs (choice of suitable partners) and smaller technology suppliers.

LAs need to consider and assess whether a large integrated contract would provide better value for money than several smaller (disaggregated) contracts. Integration of different services under different contracts could be achieved using a project manager.

It is also the case that this option may allow a LA to focus on maximising recycling and the use of low technology treatment solutions (e.g. composting) whilst leaving the development of major infrastructure for a second procurement phase when there may be greater certainty over need for residual waste treatment and the technology to undertake the treatment – with such further procurement potentially being undertaken using the PFI route which lends itself to the high capital expenditure associated with the development of such major infrastructure.

The major disincentive for this option is the lack of any PFI credits. Many LAs believe that they cannot afford the required services without such credits so opt for PFI. The PFI transaction costs, together with the desire to obtain the maximum possible PFI credits, drive LAs towards the procurement of an integrated contract. Some LAs suggested that they would be happy to consider PPP with disaggregation of contracts and prudential borrowing, if there was some form of revenue support akin to PFI credits.

It should also be noted that, following the repeal of Section 32 of the Environmental protections Act 1990, LAs could take back their waste disposal services in-house and develop parts of the required solution themselves.

The table below provides an analysis of each option for a LAWDC in a PPP procurement scenario:

Table 4 – PPP Procurement Analysis

LAWDC Option	Does it increase competition?	Can the LAWDC manage this option?
Main contractor	Yes, particularly if a range of contracts is offered rather than an integrated contract. Once again, private sector contractors may not wish to bid against a LAWDC unless they can be assured that there is a completely level playing field.	Yes, although this will depend upon the strengths of the LAWDC. For LAWDCs with a limited range of services, a disaggregated procurement scenario would allow the LAWDC to bid for those contracts where it has suitable sites/capabilities.
Partnership/joint venture	As above for main contractor, plus the inclusion of appropriate partners may result in a greater choice of technology options.	Yes. The option that NEWS are bidding for, although described as PFI without credits, may be considered to be similar to this, particularly as the tender appears to be for an interim solution, with an additional, long term tender to be offered later.
Subcontractor	Unlikely to increase competition in a municipal waste PFI procurement, however retention of the LAWDC may result in increased competition being available within the commercial waste sector.	Yes.

6. CONCLUSIONS

6.1 General Conclusions

Our analyses indicate that LAWDCs could play a significant role in providing waste management services to LAs. However, LAs see a number of barriers and need to be convinced that they can be overcome. They need to be convinced that:

- LAWDCs can offer value for money in delivering the required services.
- Risk is adequately transferred.
- Involvement of the LAWDC will not have a detrimental effect on competition.
- The LAWDC will remain viable, even if it fails to win the contract.

6.2 PFI Conclusions

It would appear that the PFI procurement option has so many barriers/hurdles to LAWDC involvement that the likelihood of a LAWDC being able to successfully bid and meet the requirements of the SOPC3 contract as a main bidder is very small. Aside from the financial and technical considerations that must be taken into account for a large integrated waste management contract, the fundamental requirement for risk transfer remains and no clear mechanism for a LAWDC to meet this requirement has been identified.

For the option of a LAWDC acting within partnership or joint venture, the advantages the LAWDC may bring to the partnership/joint venture will depend upon how the joint venture is structured, as it may provide an opportunity for smaller technology providers to enter the market if they are willing to take on some or all of the risks associated with the technology. NEWS appear to have satisfied their financiers and the WDAs advisors concerning appropriate risk transfer by using such a mechanism and negotiating a step-in clause with their bank, therefore this option would appear to be potentially available.

A third option is for the LAWDC to be offered as a sub-contractor. This option would allow the LA to retain some of the benefits of owning the LAWDC and may also allow the LAWDC to continue to develop its commercial waste business. From the LAWDC perspective, this would be likely to limit its ability to grow its public sector business as a main player but may allow it to grow its commercial business unhindered.

For a LAWDC owning LA considering the PFI procurement option, it will therefore be important to consider the potential financial and risk transfer benefits of the PFI option against the potential benefits that retaining the LAWDC may have – this will depend upon the type and scale of services provided by the LAWDC and will be different in each case. Of particular note is the concern that the disposal of the LAWDC may result in a local waste management monopoly and result in increased prices that may impact upon the whole local economy – views have been expressed that a monopoly created by a successful LAWDC would be a more "benign" monopoly than one that may be created were a LAWDC to be transferred to a PFI contractor, in that the owner of the LAWDC (the WDA) would be less inclined to exploit it's monopoly position to ensure increased financial returns at the potential expense of the local community (both social and business). It is also worth noting that several interviewees and workshop attendees (from several stakeholder groups) expressed the opinion that the PFI procurement method, involving long-term, integrated contracts, may not be truly suitable for waste management procurement, given the high risks involved in the utilisation of, in some cases, still very new technologies with uncertain future problems and the complex and changing nature of the regulatory regime for waste management. During the preparation of this report, Gloucestershire County Council withdrew from their current PFI waste management procurement project[3].

[3] See http://www.Defra.gov.uk/environment/waste/localauth/funding/pfi/pdf/gloucestershire.pdf for the Defra press release concerning this matter.

The issue of risk management is clearly one of the most significant matters concerning the ability of LAWDCs to enter into PFI procurement, either as a main contractor or in a joint venture/partnership. There are many different risks associated with waste management procurement (e.g. technology risks, service risks, planning risks) and it may be of benefit for Defra to consider if PFI risk transfer requirements can be adapted for waste management procurement, so that certain risks can be considered as acceptable/manageable by the WDA whilst others must be transferred.

6.3 PPP Conclusions

The PPP procurement route appears to provide more options for the involvement of LAWDCs, either as the main contractor or in a partnership/joint venture, due to the strict risk transfer requirements of the PFI route not applying to the process. There is still a need for the contracting LA to ensure that risks are managed and transferred where possible but there would appear to be more options available for such risk management.

The main conclusion from the workshop regarding the PPP process was that it facilitated the disaggregation of an integrated contract, as discussed in Section 5.3. Whilst it was considered that there are some potentially significant benefits to this option, it was also noted that there are potential disadvantages as well (particularly the lack of any revenue support such as PFI credits) and that LAs who are currently determining what procurement method to undertake should consider this as a potential option.

6.4 Financing Conclusions

For low risk contracting, financing is available for LAWDCs. Financing for technology is seen as high risk and is probably not available directly to LAWDCs who generally possess limited technology assets, limited experience of operating such assets and limited financial strength to support the capital requirement. Financing may, however, be accessible via a joint venture or partnership. Any technology risk may have to be supported by the parent company balance sheet, therefore there is a need for the parent company to ‘wrap’ the technology companies and take on the risk – this is a guarantee required by the lenders. Financing is available subject to funders requirements on security.

PPP procurement allows LA prudential borrowing; this has the possible benefit of lower cost finance and a lower cost of procurement.

6.5 Other Issues

In order for this study to be taken further, it is suggested that some or all of the following issues should be addressed:

- From consultations with different legal advisors during the undertaking of this study, it is clear that there are a diversity of views regarding the legality of a LAWDC taking part in PFI procurement. A formal analysis of competition law should be undertaken to clarify the pathways under which LAWDCs may operate within the marketplace.
- Some financial advisers consider that PFI is not the solution for a LAWDC as a sole bidder because they would not be able to secure the necessary funding. Under PPP, funding maybe available via prudential borrowing. This potential of this funding option should be further explored.
- The commercial viability of the LAWDCs operations in the trade waste market should be investigated. There may be a potential for the LAWDCs to develop this market to increase the competition within the commercial waste sector and increase the LAWDCs profitability to secure a continuing future under the LA. This line of business may lead to technology partnerships and a multi-activity track record, which would better place them for future procurement projects.
- In each procurement case, a risk model needs to be developed to identify how the risk flows between all parties (LA, SPV, parent companies, technology providers, subcontractors) involved in each area of procurement - PFI, PPP, JV/Partnerships and disaggregation.

- Under Section 47 of the Clean Neighbourhoods and Environment Act 2005, Section 32 of the Environment Protection Act 1990 has been repealed in October 2005 and LAs now have the option of taking waste management services back in-house. This may have significant implications for LAs that still have LAWDCs and are still to undertake procurement of waste management services, for example the LA may wish to take back its waste disposal services in-house, although returning the assets and staff of a LAWDC to a LA is likely to be complex. Further detail on the potential implications of this change can be found in the Defra document "Clean Neighbourhoods and Environment Act 2005 – Interim Guidance for Measures commenced on 18 October 2005 (http://www.Defra.gov.uk/environment/localenv/leqbill/051018-interim-guidance.pdf).

Appendix 1 – Invitees and Consultees

The following organisations were invited to take part in this study. Those highlighted in bold text did take part in the consultation exercise.

4Ps
Ashurst
City of York Council
Cornwall CC
County Environmental Services
Coventry City Council
Coventry & Solihull Waste Disposal Company
Cumbria CC
Cumbria Waste Management
Deloittes
Durham CC
Englefield
ESA
Eversheds
E&Y
Greater Manchester Waste
Greater Manchester Waste Disposal Authority
HM Treasury
Inniesfree
KPMG
LGA
Merseyside Waste Disposal Authority
Mersey Waste Holdings
Nabarros
NIB Capital
Norfolk CC
Norfolk Environmental Waste Services
North Yorkshire CC
Premier Waste Management
PWC
RBS
Sharpe Pritchard
SITA
Somerset CC
Suffolk CC
Surrey CC
Viridor
Wyvern Waste Services
Yorwaste

Appendix 2 – LAWDC Summary Table

LAWDC	Main Assets (Owned)	Waste Handled (approx) (tpa)	Turnover (approx)	Current Status
CES	2 operational landfills 4 closed landfills 1 transfer station	250, 000 tpa for Cornwall CC 100,000 tpa commercial waste	£17M pa	Cornwall CC currently undertaking PFI procurement, with transfer of LAWDC assets.
C&S Waste	1 incinerator 1 civic amenity site 1 closed landfill	220,000 tpa to incinerator from Councils 35,000 tpa through CA site, of which 8,000 tpa sent to incinerator	£10M pa	Coventry City Council have submitted PFI outline business case, however targets are now being met.
Cumbria Waste Management	Plant, including vehicles and a leachate treatment plant. All sites leased.	220,000 tpa	£12M pa	Cumbria CC tendering for integrated waste management contract by PPP. Options to sell LAWDC or retain as landfill provider.
Greater Manchester Waste	Real estate or leasehold for all plants except energy from waste plant	1.2 – 1.4M tpa	£100M	Greater Manchester WDA undertaking PFI integrated waste management procurement – likely to be share sale of LAWDC with the contract
Mersey Waste	Some land assets Part ownership of landfill site	950,000 tpa	£40M	Merseyside WDA have just appointed advisors to assist in procurement process. Initial advice has been share sale of LAWDC with the contract
NEWS	1 materials recovery facility 1 civic amenity site 3 closed landfills	205,000 tpa	£11-12M	Norfolk CC currently undertaking disaggregated PFI procurement with no credits. NEWS, via a joint venture, one of two bidders remaining for interim contract.
Premier Waste Management	2 operational landfills 1 aerobic digester I depot	1M tpa	£38M	Durham CC not currently undertaking procurement process.
Wyvern Waste	5 landfill sites 4 civic amenity sites 3 transfer stations (1 closed) 1 materials recovery facility 3 windrow compost sites 1 in-vessel composting plant	490,000 tpa	£30M	Somerset CC currently intend to sell LAWDC to preferred bidder under PPP procurement. PPP contract drafted to be SOPC3 compliant.
Yorwaste	Freehold owner of greenfield site with planning permission	1M tpa	£17M	LAWDC has recently successfully tendered for North Yorkshire CC landfill contract to 2010. Tender had some similarities to PFI. NYCC and CYC are considering future options for procurement, with PFI the likely mechanism.