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TO: JOINT WASTE DISPOSAL BOARD  
8 APRIL 2016

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**CONTRACT GUIDANCE REPORT – PAYMENT MECHANISM**  
**Report of the re3 Strategic Waste Manager**

**1 INTRODUCTION**

- 1.1 The biennial audit of the re3 contract (undertaken in 2015) identified that it would be helpful if a guidance document were produced. A contract guidance report was presented to the Board at the January 2016 meeting. The purpose of this report is to provide guidance on the Payment Mechanism.

**2 RECOMMENDATION**

- 2.1 **That Members note the contents of this report.**

**3 ALTERNATIVE OPTIONS CONSIDERED**

- 3.1 Not applicable.

**4 REASONS FOR RECOMMENDATION**

- 4.1 This report contains no decisions for Members, only briefing.

**5 BACKGROUND INFORMATION**

**Background**

- 5.1 The re3 PFI Contract commenced on December 4<sup>th</sup> 2006 following over a year of intensive negotiations. The Contract was initially valued at £611m over its 25 year term.
- 5.2 The re3 councils were successful in securing £37m support for the project through the Private Finance Initiative (PFI). In cash terms, as the councils chose to receive the support throughout the life of the contract, the support equates to £74m and very broadly to £1m per council per annum.
- 5.3 The current annual cost of the contract is £26m. Management of the Contract (additionally including internal and statutory reporting, financial management and monitoring of KPIs) is delivered by 2.6 FTE.
- 5.4 Recommendation 1 in the report on the 2015 audit of the re3 contract advises that there is a need for guidance for Members and senior officers. It says:
- ‘...it would be helpful to produce a consolidated guidance document which explains the relationship between elements of the Contract’.*
- 5.5 The recommendation was accepted, by the prevailing Project Director and a timetable for the production of such guidance set for the first Joint Waste

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Disposal Board meeting of 2016.

- 5.6 This report contains advice on the Payment Mechanism, the contract document which sets out the calculation of the Unitary Charge payable by the Councils to the Contractor.

### **Guidance**

- 5.7 This report provides a consolidated source of guidance for Members and Senior Officers of the re3 councils on the Payment Mechanism. The report constitutes neither legal advice nor advice on managing the contract or Contractor.

- 5.8 The monthly Unitary Charge is based upon a Waste Flow Forecast (of tonnage) that is agreed between the Councils and the Contractor in advance of the contract year.

- 5.9 The Unitary Charge comprises the following payments:

- a) the Baseline Payment
  - b) the Recycling Payment
  - c) the Composting Payment
  - d) the Energy Recovery Payment
  - e) the Landfill Payment
  - f) the Beneficial Use Payment
  - g) the CA Site Payment
  - h) the Waste Minimisation Fee
  - i) the Monthly Estimated Recyclate Income Compensation Payment
  - j) Passthrough Costs
  - k) the Extended Hours Payment
  - l) the Rejected Load Payment
  - m) the Contamination Payment
  - n) the First Annual Reconciliation Payment and
  - o) the Second Annual Reconciliation Payment
- Less
- i. Excess Profit Share in respect of the previous Contract Year
  - ii. the Royalty Payment and
  - iii. the Quarterly Reconciliation Payment

### **Baseline Payment**

- 5.10 The Baseline Payment is applicable to every tonne of contract waste that is delivered to the re3 Project Facilities (the Transfer Stations, the MRF and the Longshot Lane and Smallmead Recycling Centres/HWRCs).

- 5.11 The Baseline Payment is subject to a guaranteed tonnage of 190,000 tonnes per year. The guarantee is required because the Baseline Payment is the means of the Councils repaying the costs of building the re3 facilities to the Contractor.

- 5.12 As noted in the Contract Guidance report, the re3 councils secured PFI credits

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in order to fund the construction costs, which are spread over the life of the contract.

- 5.13 Since commencement of the contract in 2006, annual contract waste has only been below the guaranteed threshold once – in 2012/13 during the economic crisis.
- 5.14 Contract tonnage in excess of the 190,000 tonne threshold is charged in banded rates, which are significantly reduced costs per tonne.

### Recycling Payment

- 5.15 The Recycling Payment is calculated based upon the number of tonnes of contract waste that are recycled each month plus recycling haulage costs.
- 5.16 Recycling tonnage is collected at bring banks, the Recycling Centres (HWRCs) and by the council kerbside collections (excluding any contaminated/MRF-rejected tonnage).
- 5.17 As with the Baseline Payment, recycling tonnage is charged according to weight bands, although there is no minimum tonnage requirement.
- 5.18 Haulage is charged on the tonnage of kerbside collected recyclables that are delivered by the Councils to Longshot Lane and then transported by the Contractor to the Smallmead MRF.

### Composting Payment

- 5.19 The Composting Payment is calculated based upon the number of tonnes of contract waste that are composted each month plus haulage costs.
- 5.20 Composting tonnage is collected at the Recycling Centres, by the kerbside collections and by the Councils' parks/grounds maintenance teams.
- 5.21 Composting tonnage is charged according to weight bands, and there is no minimum tonnage requirement.
- 5.22 Haulage is charged on every tonne of contract waste that is sent for composting.

### Energy Recovery Payment

- 5.23 The Energy Recovery Payment is calculated based on the tonnage of contract waste which is sent to the Lakeside EfW facility each month.
- 5.24 Tonnage sent to Lakeside is subject to an annual maximum of 61,200 tonnes. In 2011 the Councils procured an additional 10,000 tonnes per annum of EfW capacity.
- 5.25 EfW tonnage is charged at a fixed gate fee subject to annual inflationary

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increases.

- 5.26 Haulage is charged on every tonne of contract waste that is sent to EfW (on both contracts).

### Landfill Payment

- 5.27 The Landfill Payment is calculated based on the tonnage of contract waste which is sent to landfill each month.
- 5.28 The charge is comprised of Landfill Tax, the landfill gate fee and the haulage fee. Haulage is charged on every tonne of contract waste that is transported to landfill by the Contractor.
- 5.29 The Payment Mechanism sets out the annual landfill gate fees for the term of the contract, and these are subject to contractual inflationary increases.
- 5.30 The council is entitled to make a Recovery Performance Deduction from the Landfill Payment where the contractor sends more waste to landfill than the calculated maximum tonnage to landfill.

### Beneficial Use Payment

- 5.31 The Beneficial Use Payment is calculated based on the tonnage of contract waste at the Recycling Centres that is diverted for reuse – namely hardcore and soil.
- 5.32 The charge is a fixed rate that is subject to contractual inflationary increases each year.

### CA Site Payment

- 5.33 The CA Site Payment is paid to the contractor each month for the operation of the Longshot Lane and Smallmead Recycling Centres (previously known as CA Sites/HWRCs).
- 5.34 This is a fixed payment that is subject to contractual inflationary increases each year.

### Waste Minimisation Fee

- 5.35 At the commencement of the contract, £100,000 per annum was put aside from the councils payments to fund education and waste minimisation activities. A further £50,000 was put aside to fund staff costs for the two posts.
- 5.36 From the start of the contract until January 2011 the waste minimisation function was carried out by the contractor. At this point the remaining Waste Minimisation Officer left, and the arrangement was reviewed.
- 5.37 In July 2011 the re3 Board took the decision to utilise their own resources to undertake waste minimisation activities, and reduced the Waste Minimisation

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Fee to £50,000 per year (indexed annually).

- 5.38 In 2015 the councils appointed the re3 Communications and Marketing Officer. As the contractor is no longer providing the waste minimisation service, there is no longer the need to pay the full Waste Minimisation Fee in the Unitary Charge.
- 5.39 A Change Notice has been agreed which makes the provision to pay the contractor a Waste Minimisation Fee of £1 per annum. This is in order to retain the contractual mechanism should it be required in the future.

### Monthly Estimated Recyclate Income Compensation Payment

- 5.40 The contractor is required to provide an estimate of the amount of Recyclate Income Compensation Payment forecast to be due in the contract year. The Monthly Estimated Recyclate Income Compensation Payment is equal to one twelfth of the annual estimate.
- 5.41 Where income is above the sharing threshold the councils will receive a 40% share. Where income is below the sharing threshold there is potential for the councils to have to compensate the contractor (on the basis of lower tonnage or poorer composition).

### Passthrough Costs

- 5.42 Passthrough Costs are primarily charges for disposing of wastes that are not subject to the types of charges described above, typically hazardous wastes deposited at the Recycling Centres (e.g. plasterboard, asbestos, paint).
- 5.43 These types of hazardous wastes are charged at spot (i.e. not fixed) prices, and the contractor is required to use reasonable endeavours to minimise processing costs to the councils.
- 5.44 Passthrough Costs also cover Additional Works charges, such as additional emptying of bring banks and installation and operation of new bring bank sites.

### Extended Hours Payment

- 5.45 The contractor is entitled to charge for any period of extended opening of the facilities that is requested by the councils. Extended opening is typically required following Bank Holidays when the kerbside collection crews work different hours to 'catch up'.

### The Rejected Load Payment

- 5.46 Green waste and kerbside collected recycling are subject to a Waste Acceptance Protocol whereby if a council-delivered load is too contaminated for processing to be viable, the contractor can reject the load and charge the councils for handling.

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- 5.47 In the early years of the contract the contractor did on a few occasions express intent to reject a small number of loads but the re3 Project Team managed this and to date we have not had a Rejected Load Payment.

### The Contamination Payment

- 5.48 The councils pay the Contamination Payment to the contractor in respect of the additional processing of contaminants present in the kerbside collected recycling.
- 5.49 The charges per tonne are graded, depending upon the level of contamination assessed by compositional surveys to be within the collected recycling. The councils are currently paying the highest rate per tonne due to the levels of contamination.

### Performance Deductions

- 5.50 The Performance Mechanism of the contract has 71 performance standards against which the contractor's performance is monitored.
- 5.51 When performance failures exceed the contractual tolerance, the councils are entitled to apply Performance Deductions.
- 5.52 The most frequent cause of Performance Deductions is 'turnaround failures', where council-authorized vehicles are held on site in excess of 20 minutes, usually due to site congestion.

### First Annual Reconciliation Payment

- 5.53 The First Annual Reconciliation Payment is undertaken following the end of each contract year and comprises the Recovery Gainshare and the actual Recyclate Income Compensation Payment, less the Estimated Recyclate Income Compensation Payment.
- 5.54 The Recovery Gainshare entitles the contractor to a 50% share in any net council share of Landfill Tax savings, when the actual tonnage of waste set to landfill is less than a calculated Target Landfill Tonnage.
- 5.55 Estimated Recyclate Income Compensation Payments are compared against the actual Recyclate Income Compensation Payments, and a reconciliation payment is made (this can be to or by the councils, depending on whether actual income earned exceeded the forecast).

### Second Annual Reconciliation Payment

- 5.56 The Second Annual Reconciliation Payment is undertaken following the end of each contract year and comprises the Diversion Gainshare less the Annual Diversion Performance Deduction.
- 5.57 The Diversion Gainshare entitles the contractor to a share of income earned from the sale of surplus LATS (Landfill Allowance Trading Scheme) permits.

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- 5.58 The cessation of the LATS scheme in 2012/13 means that this calculation is now obsolete.
- 5.59 The Annual Diversion Performance Deduction entitles the councils to a deduction from the Landfill Payment when the councils incur additional LATS costs as a result of sending more waste to landfill than the calculated target tonnage.
- 5.60 As above, with the LATS scheme no longer in operation, this calculation is no longer required.

### Excess Profit Share

- 5.61 The Excess Profit Share mechanism ensures that contractor profits beyond those modelled at the time of contracting are shared with the councils.
- 5.62 Where contractor profits are 1.5 times above expected, the councils are entitled to 25% of the excess.
- 5.63 Where contractor profits are twice that expected, the councils are entitled to 75% of the excess.

### Royalty Payment

- 5.64 The contractor pays the councils a Royalty Payment in respect of Third Party (i.e. non-council) waste that is received at the facilities.
- 5.65 This payment is subject to a cap of £50,000 a year.

### Quarterly Reconciliation Payment

- 5.66 Following the end of each quarter, the contractor calculates the Quarterly Reconciliation Sum, which is the sum of the quarterly charges based on the tonnage forecast, less the sum of the quarterly charges based on the actual tonnages received.

## **New Developments**

- 6 A successful trial was undertaken in autumn 2015 to send street sweepings for processing, which results in a significant proportion being diverted from landfill, and at a lower cost to the councils. A Change Notice has been agreed and a new section will be introduced to the Payment Mechanism to capture sweeping tonnage and processing costs.
- 6.1 Another trial is being undertaken to send residual material from the Recycling Centres to FCC's MRF in Sutton Courtenay. A small amount of the material is separated for recycling and the remainder is used for RDF (Refuse Derived Fuel), thereby diverting this tonnage from landfill at a lower cost. If this arrangement is made permanent then a new section for RDF will be added to the Payment Mechanism.

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### 6 **ADVICE RECEIVED FROM ADMINISTERING AUTHORITY**

#### Head of Legal Services

6.1 None

#### Corporate Finance Business Partner

6.2 None

#### Equalities Impact Assessment

6.3 None.

#### Strategic Risk Management Issues

6.4 None from this report.

### 7 **CONSULTATION**

#### Principal Groups Consulted

7.1 Not applicable.

#### Method of Consultation

7.2 Not applicable.

#### Representations Received

7.3 Not applicable.

#### Background Papers

Audit Report, 16<sup>th</sup> October 2015

Contract Guidance Report, 15<sup>th</sup> January 2016

#### Contacts for further information

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