INVESTMENT OPPORTUNITIES: MUNICIPAL WASTE AND PFI

Sofitel St. James, London
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Conference Report

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Session One – The £10 billion Opportunity

Municipal waste: progress and potential
Environment Minister, Elliot Morley

Overview:

Almost 28 million tonnes of municipal waste are produced each year in England. Nearly 80% of this is currently being sent to landfill sites – a waste of valuable resources, and a major environmental issue.

European legislation is driving a more sustainable approach to managing waste and the Government is determined to tackle reliance on landfill and deliver change. Securing sustainable waste management is a challenge, but it provides major opportunities for the private sector.

The EU Landfill Directive is the biggest policy development in recent years, which restricts the landfilling of biodegradable household waste.

Considerable progress needs to be made. Increasingly the business of collection, management and disposal of waste is contracted out to private sector companies. To meet our targets, greater investment is needed in these kinds of services – up to £600-700m per year over the next 10 years.

The Government sends clear signals about the need for change and extra resources have been provided for a more sustainable strategy. These extra resources include £1.1 billion extra provision for local authority waste services, which are spent mostly through contracts with the private sector.

This was announced as part of the 2000 Spending Review (SR), and a further £671m in SR2002. SR2004 provided further resources to help local authorities to invest in value for money waste disposal facilities. An additional £275 million in Private Finance Initiative (PFI) credits will be available over the Spending Review period, over and above the £355 million available from SR2002.

In addition to providing funding, Government has established the Waste Implementation Programme (WIP). WIP is devoting over £150m from 2003 to 2006 to strategic measures helping authorities to divert waste from landfill. Government has also established the Waste and Resources Action Programme (WRAP) to ensure a rigorous focus on end market creation.

To date, nine waste PFI projects have been signed and a further eight are in procurement. These projects represent over £1 billion worth of capital investment and total contract values of £9.5 billion. So, there is clear evidence of a growing demand for PFI on the part of local authorities.

However we are aware of issues that can be difficult for private sector investors to get involved in waste management. Issues such as planning delays, public concern due to potential health effects, insufficient data and uncertain markets are some of the reasons we have identified.
Session Two – Engaging with Waste PFI: How and Why?

The rise of waste PFI: in theory and in practice
Samantha Gain: 4Ps

Overview:

- Joint working & partnership key with good working relations between different waste stakeholders so that all could be kept together under one contract.
- Trying to make waste an “apolitical” issue
- New model of ‘Regional’ based PFI projects beginning to appear and be tested, for example Kirklees, Calderdale and Bradford.
- Must make the Business Case ‘fit for purpose’.
- 4 Ps role is ‘to try to assist the market and authorities to come to a contract that they are happy with, is realistic, can inform future deals as a way of going forward.’

PFI overview: how to engage
Ron Bates: Defra

Overview:

The process can be viewed as going through 6 key stages.
In summary these are:

Expression of Interest (EoI): This is the first stage and it is an opportunity for a local authority to advise us of their longer term intentions, what they envisage as the preferred way forward and what they have put in place to address those things. Here we are testing a number of things such as the validity of their proposed solution, what level of strategic work they have undertaken, what the level of political buy in is and what wider consultation has been undertaken with key stakeholder groups.

Outline Business Case (OBC): Once satisfied that the basic building blocks are in place, authorities will progress to a fuller exposition of their project. This is a very much more detailed and costed business case which will be further tested on the issues covered at the EoI and is where the authority will demonstrate that pursuing their solution with a private sector partner will deliver value for money (vfm) as compared with the authority delivering the project in house. It is also tested with regards to financial deliverability and how well the output specification is defined; i.e. is the authority clear on what it is asking the market to deliver? This is undertaken in 2 parts. Firstly the sponsoring department will review the OBC and if satisfied will seek ministerial approval for the project. Once that approval is received, the project then moves on to review by the Project Review Group, a Treasury chaired
cross departmental group. Once approved at this stage, the PFI credits are awarded in principle.

**Pre-procurement**: This is what should be the relatively short stage between OBC approval and issue of the project notice in the Official Journal of the European Union or OJEU. This notice should normally be largely in place by PRG approval of the OBC.

**Procurement**: Definitely the longest and most intensive stage of the project. This will include a number of stages itself, including ITN, (possibly) ISOP, BAFO, preferred bidder and then the long haul working through the detail of direct agreements, project agreements, the payment mechanism, etc.

**Contract completion**: And finally to contract close. All the hard work pays off for both sides. What is delivered is the next step in a developing market which will go on to deliver partnership working to the benefit of the public and private sector.

Earlier this year two studies were undertaken to look at what the issues were in this sector for banks and potential new entrants.


Forward deal flow for the current spending review period, which takes us to March 2008. This reflects where the various authorities are in terms of preparedness and therefore when they are likely to go to market. These are indicative and it is likely that there may be some movement by individual authorities, but this represents those authorities furthest progressed towards a PFI procurement. Furthermore, the lack of dates against the last line indicates that these three local authorities represent a potentially new approach to PFI in waste. 4Ps and Defra are starting to consider models for regional procurement and this group of local authorities may well be the first to take forward a procurement based on some form of regional procurement model.
### Forward Deal Flow in Waste PFI

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<td>Kirklees, Calderdale &amp; Bradford</td>
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### Session Three – Responding to key issues

**Making projects fit for market: providing the tools**

**Samantha Gain: 4Ps**

**Overview:**

#### Bid criteria and delivering successful projects

- Justified as part of strategic review and options appraisal
- Clearly set out structure for Expression of Interest and Business Case
- Realistic assessment of costs, risks and technology
- Meets national and local objectives setting stretched targets
- Partnering options and deliverability
- Early private sector involvement, market soundings
- Creating a level playing field e.g. sites
- Project management arrangements
- 4ps supporting local authorities in preparation

#### Joint Working and Partnerships in Waste

- Waste strategies as the catalyst for joint working
- Recognised need for mutual support in meeting long term targets and delivering sustainable solutions
- Focusing on project requirements and developing options that meet partners requirements
- Clear understanding of cost profiles for each partner
- Political and stakeholder buy-in
- Integrated and semi integrated projects
• Making sure partnerships can deliver
• New procurement models
• Key issues for a successful procurement

**Business Case must be fit for purpose**

• Reference Project is deliverable including sensitivity analysis
• Timescales and resourcing to deliver the project
• Waste Strategies and Waste Local Plans
• Site availability and planning risk
• Project outputs and technology are understood by all parties
• Costing and allocation of risk e.g. third party markets
• 4ps supporting procurement and developing Best Practice

**Making projects fit for market: the project review process**

**Michael Gerrard: PUK**

**Overview:**

• PRG was created to respond to issues by private sector and is a PPP itself.
• Its not meant to impose ‘the heavy hand of the centre’ on local authorities but to help them by providing an ‘enabling framework’.
• Introduced to give market and local authorities confidence that intended procurements were likely to reach a successful conclusion
• Compulsory Gateway review to establish commercial viability of all Local authority proposed PFI schemes (that require PFI credits), prior to procurement launch.
• Provides early check of the likely availability of funding and associated conditions before major procurement expense is incurred
• PUK act as ‘a quality control’, a ‘health check’ and 200 local PFI schemes have passed through the process since its start.

**PFI and technologies: proving the potential**

**Dave Brooks: Defra**

**Overview:**

• ‘New technologies’ but only ‘new’ in the sense of new to the England as often they are already being used successfully elsewhere.
• This work is not specifically PFI but has a big impact on PFI and in 2 to 4 years time would hope that these new technologies would and could be chosen for PFI projects.
• Risk is a major issue and lack of funding contributes to poor engineering and greater risk. This in turn leads to serious lack of people willing to insure, and a seriously high premium.
• One way of getting waste onto the ‘apolitical agenda’ would be to get local authorities to agree it as a part of their Community Agenda Strategy that remains in place in spite of ‘colour’ changes at elections.
• Need for ‘joined-up’ thinking and involvement of all regional parties including Health Authorities.
• Data centre crucial as the provider of ‘impartial information’ regarding new technologies.

Closing the loop: developing sustainable markets
Steve Creed: WRAP

Overview:

• In first 3 years, responsible for 3.7m tonnes going to be recycled per annum. However “until bought, it is not really recycled.”
• Closing the Loop is about doing more with less, and ‘sustainably’ means both environmentally and economically sustainable schemes.
• Price Stability is key to successful end market and market pricing report, to which sixty members have already signed up to, has helped price stability and visibility. Could consider these prices in value of PFI project future projections.
• Reprocessing is a particularly challenging area and the Recycling Fund has been set up to prove both government commitment and financial viability.
• Key to delivering end market is to compete on price, quality & availability, not on ‘recycled’ properties. Rather than going for 100% recycled products try to work with what is already out there and inject say 10/20% of recycled content into it i.e. the construction industry.
• Market interventions will lead to demand for recycled materials increasing as the above measures start to deliver growth in the market. This increased demand will be accompanied by an increase in the price that the materials extracted from the waste stream will command.
• The challenge will be to match growth of supply and demand to ensure an efficient transition to sustainable markets. WRAP is now working on methods of assessing and modelling these market transitions to inform future strategies.

Better data, better planning: addressing other barriers
John Burns: Defra

Overview:

• The Minister identified issues that can be difficult for private sector investors to get involved in waste management, such as planning delays, public concern due to potential health effects, insufficient data and uncertain markets are some of the reasons we have identified. We have started to make headway on tackling these issues.
• Defra has published a major report on the health and environmental impacts of waste, peer reviewed by the Royal Society. The Government’s advice is that the report gives us sufficient confidence in
our current policies for local authorities to press ahead urgently with the
task of approving planning applications for new waste management
facilities in line with the hierarchy of waste disposal with minimisation at
the top and landfill at the bottom.

- Government will shortly issue strengthened advice on the operation of
  the planning system, helping to ensure all required facilities for
  recycling and residual waste management can proceed. During the
  Autumn, Defra and ODPM will be consulting stakeholders on a revised
  Planning Policy Statement (PPS10) on Waste Management.
- Defra have now launched a major public consultation exercise to
canvass views on a national 3-year waste data strategy. The strategy
sets out proposals for delivering more accurate, complete, timely and
consistent data across all waste streams.
- Need to ‘move away from landfill to an industry based increasingly on
  engineering & technology’.
- End markets for Refuse derived fuel: Consideration of Energy-from-
  Waste eligibility is included within the 2005 Review of the Renewables
  Obligation.
Session Four – Discussion and Feedback

Panel Discussion with:
John Burns, Director of Waste Implementation Programme, Defra
Steve Creed, Director of Business and Procurement, WRAP
Fred Portnell, 4P’s
Michael Gerrard, Deputy Chief Executive, PUK
Peter Calliafas, Head of the Environmental Services Team, Barclays

Overview:

In the situation when clients have not procured anything on a big scale. What is being done to address gaps in local authority procurement skills?

Defra recognises that this has been a major issue in the waste sector and is beginning to address this in a number of ways. One of the things we are doing through the Local Authority Support Unit (LASU) is providing consultancy support to local authorities to help them map out realistic and deliverable procurement strategies. Also, using WRAP funding, the 4Ps have led a piece of working, in consultation with local authorities and the private sector, to develop a procurement pack for waste PFI which is an important first step in providing standard guidance to local authorities. Further work is planned to build on this and to move to a waste specific standard contract over the next 18 months or so; sooner if at all possible.

We recognise that it is important not to lose the experience acquired by local authorities that have undertaken or are undertaking PFI procurements and that there are also opportunities for local authorities to learn from each other. Accordingly we are working with the 4Ps to deliver networking events for local authorities which will provide such an opportunity.

By 2007/08, Defra will help local authorities to deliver £300 million worth of efficiency gains on waste and street cleansing services. While the delivery of efficiency gains rest with authorities themselves, Defra is committed to assisting local authorities to secure these savings, mainly by promoting more effective joint working, promoting best practice and standardisation of procurement operations. The efficiency agenda means it has never been more important to get this support right, and give a strong additional focus to the kinds of support that WIP is already seeking to provide.

It is frustrating when you have to reinvent the wheel during every PFI project. Would Defra investigate the potential to set up ‘a centre for waste procurement excellence’?

This issue is currently being addressed. We are in discussion with ODPM colleagues on how this might be implemented, possible through the regional
centres of excellence currently being established, and are seeking funding to put this in place.

*In the procurement pack one of the case study used is Leicester. Leicester didn’t involve banks and there were issues surrounding RDF, does this offer a good case study for PFI?*

Leicester was used as an example of an operational project that is beginning to deliver as envisaged. This is a project that has experienced some problems, albeit not directly related to the contract itself, but which has shown that PFI can deliver in waste, even in adverse circumstances. More generally, the procurement pack aims to flag up points of standardisation while still recognising there are no two projects the same.

*Looking at the number of procurements coming up is there anything Government can do to minimise complications, for example unrealistic elements need to be recognised and addressed.*

Certainly government recognises complications exist and, as previously referred to, is taking steps to address these. Clearly there are risk areas where local authorities may have had an unrealistic view of what the private sector could reasonably take on in whole. These are areas where we are working with local authorities, often well before the EoI stage, to ensure they are doing more work up front to, as far as possible mitigate such risks. However, clearly the more risk that is left wholly in the public sector, the less value there is in using a PFI route. That is why it is important that the private and public sectors work together to establish a reasonable risk sharing approach and we would look to the private sector to play its part in that dialogue.

Furthermore, in assessing the EoIs and OBCs that we receive from local authorities, we are very thorough in testing the proposed targets and preferred options in terms of realism, viability, affordability and bankability.

*Delegates were encouraged to see the forward deal flow, however with the additions from the spending review there were concerns that the figures didn’t add up to enough to cover the existing projects, let alone new ones How is this going to work?*

It has not generally been the case in the waste sector that PFI credits were expected to fully cover the capital costs of projects. Local authorities have to provide Commitment and funding to the table as well and that is why we place much importance on the affordability of projects when they are presented to Defra. A further consideration is that PFI will not be the only route of delivery looking ahead. Certainly government is considering alternative models, as the financial market may well be, looking at alternatives such as PPP/JV, etc. It may also be that the new prudential borrowing regime will offer local authorities another route for procuring large projects in the future.
Delegates thought there was a need for the 4Ps procurement toolkit to be revised due to best practice moving on at a rapid rate.

As referred to earlier, the current thinking at Defra and the 4Ps is around revisiting the procurement pack in late 2005 when three or four more deals have closed, although we are considering ways in which this can be accelerated in the mean time.

It was mentioned earlier that you want to make the issue of waste apolitical. What is being done to train local government on waste issues?

This is being addressed on a number of fronts. Defra, through the WIP is making itself more visible and is talking with local authorities at events such as the Local Authority Recycling Advisory Committee (LARAC) conference. We are also, along with the 4Ps, prepared to meet with and brief members and relevant government committees on the issues in waste and what we are doing to address them.

Better informed decision making at all levels needs more information and, in addition to the above, we are making more information available to local authorities and the industry through the New Technologies Supporter Programme, which aims to address the perceptions that some people have about this area.

The Local Authority Support Unit has carried out work to assist local authorities in the procurement of waste services, having established that the successful implementation of well developed waste plans relies on being effectively translated into contracts. However, a wide variation in the quality of procurement projects is evident across the country, which in turn has led to a wide variety of costs and outputs delivered in Local Authority waste management services. We are now experiencing the most challenging market conditions seen in municipal waste in recent times.

As the transition from one contract to another is the key point at which service improvements can easily be specified, the effectiveness and strategic soundness of procurement projects are critical to meeting the Government’s objectives both in the short and long term. Therefore, the Local Authority Support Unit initiated two significant projects to identify support needs in relation to procurement and develop a toolkit, based around the process of designing contract documents and evaluation criteria, specifically geared around the needs of UK municipal waste managers based in England.

The Local Authority Support Unit projects are a ‘Procurement Support Needs Analysis’ study; and a ‘Waste Procurement Toolkit’ (published January 2005), the outputs of which are located on the Local Authority Support Unit website at [http://lasupport.defra.gov.uk/](http://lasupport.defra.gov.uk/), Support Products/ Toolkits - procurement.

Local politics can be a particular barrier, especially in 2 tier areas. This is being addressed through the requirement for local authorities in those areas to work together in developing their Joint Municipal Waste Management
Strategies. We are constantly looking for other levers to influence and encourage greater partnership working between local authorities within and across recognised boundaries.

*What is the government's stance on incineration?*

Government supports the use of incineration with energy recovery, for the treatment of residual waste after recycling, or where materials cannot be safely or practically re-used or recycled. Incineration with energy recovery is acknowledged to be a viable waste management option by its inclusion in the waste hierarchy, below recycling and composting, but as a more sustainable option than disposal for example at a landfill site.

The message of some form of energy from waste (EfW) solution having a role to play in the overall picture was one which was emphasised in Elliott Morley's forward to the recent Review of Environmental & Health Effects of Waste Management in which he said that we must acknowledge the role of incineration with energy recovery as a sustainable waste management option although the priority must be waste minimisation, reuse and recycling.

The Report concludes that, on the evidence from studies so far, the treatment of municipal solid waste has at most a minor effect on health in this country particularly when compared with other health risks associated with ordinary day to day living. This includes incineration and the other energy recovery options.

*Will the Clean Neighbourhoods Bill revoke the Environmental Protection Act regarding whether local authorities will be able to tender for their own contracts?*

With the repeal of the divestment provisions in the Environmental Protection Act 1990, waste disposal will be treated in the same way as any other local authority function under Best Value. A local authority could therefore tender for one of its own contracts or bring its waste disposal function back "in house" so long as it satisfied Best Value requirements.

*In terms of deal flow and capacity in the market, many local authorities are moving towards 2010 like “rabbits in the headlights”, what is Defra doing to stop local authorities making rushed decisions?*

We recognise the importance of local authorities making informed decisions about the medium and long term approach on waste management in their areas. Defra and the 4Ps are providing support and guidance for local authorities to make better decisions. This includes working with authorities months before they submit EoI proposals to Defra.

*Regarding timescales, the procurement time in PFI is about 2 years, so for the local authorities that are tendering now, how will the facilities be ready by their target dates given the existing planning regime, and what are Defra doing to...*
educate the public not just about the importance of recycling but also what needs to be built to deal with their waste and collected material?

Some local authorities are bravely tackling the issue head on, for example, all local authorities are encouraged to go out to public consultation on issues as broad as their Joint Municipal Waste Management Strategies and as specific as what solutions and technology should be applied and on what sites. This is happening variously in areas such as Cheshire, Greater Manchester, Shropshire, Norfolk, etc. Through working with colleagues at the ODPM and feeding into the policy development and consultation process, we hope the revision of PPS10 planning guidance along with the review of Waste Strategy 2000, the planning process will become more streamlined and therefore quicker and simpler.

Also WRAP, on Defra’s behalf, have launched a £10million Recycle Now multimedia campaign with the strap-line “the possibilities are endless”. There are avenues to move in stages with the message, for example to a waste minimisation message or what processes our waste goes through to be recycled.

There is also an issue of social education that has to be addressed – it is unacceptable that we are a throwaway society. We need to view our rubbish as a resource – until we change the terminology, behaviour will remain unchanged. To address this issue, Defra are beginning to explore, with the private sector, how we might develop and move forward the public debate on waste, putting it on a more informed footing then has been the case in the past.

*The best practice of PFI from OJEU to completion is 12months, can the waste sector learn lessons from this?*

There are lessons to be learnt from more mature PFI sectors, such as education and health. Although there are other factors to consider in Waste PFI, we can use the understanding that has developed over the last 5–10 years, although there will still be issues to catch us out that haven’t previously been considered. In considering waste as a sector to engage with, there are concerns from the construction industry that waste is an immature industry and that there are, better other options such as hospitals, schools and roads. Again this is recognised and Defra are addressing through measures such as the development of the procurement pack and the future work on a waste specific standard contract, working with the private sector on developing a risk allocation model that ensures risk is placed with the partner best placed to manage it, plans for greater networking, etc.

*Will WRAP be looking at markets for RDF?*

RDF is currently poorly defined and there are several possible outputs from other waste management processes that can fall under this heading. Through the work of the Demonstrator Programme and the Data Centre it is hoped that
there will develop a far clearer understanding of the types and quality of RDF that can be produced.

Again it comes back to definitions. At present RDF is classed as a waste product, but it is not. It is a product and it needs standards. This distinction is one that is recognised across Europe; for instance, the Italians are exporting it to Germany to use in power stations. We cannot commit the ultimate marketing sin by developing the product then trying to find a market for it. We must discover the market then develop the product to suit that market.

The EA have been charged with finding out about this and will be reporting back before Christmas. In the mean time, WRAP do not cover RDF but are focused on their 6 priority materials, and Defra will continue working with the DTI looking at energy-from-waste in their forthcoming Review of the Renewables Obligation.

Conclusions and Observations from the audience:

There is a lack of capacity in the industry in terms of companies involved, level of finance available to the sector and the number of advisors available to the sector, technical, financial and legal.

There is a lack of expertise in local authorities. There is a need to focus investment and training for local authorities not just on procurement but on ‘delivery’.

There is a need to start engaging the public with the reality of new waste facilities coming their way as the present debate, besides Cheshire, is being narrowly confined to interested parties. Technologies may prove to be bankable but we need to work with the public and communities to get them built. There is an urgent need to start an informed public debate about the waste facilities required to manage the volume of waste collected.

It is about time the public recognises the cost of waste. Waste is a utility and should be apparent like the police of fire services. There is a need to move waste out of hidden pages of council tax to the front of people’s and local authority’s minds as PFI credits will not be enough, and costs of projects will be more than local authorities will expect.

LATS should help to bring waste out of the environmental agenda of local authorities and into the financial portfolio – as well as generally raising the profile of waste.