

## Report of the Director of Environment and Neighbourhoods

### Report to the Executive Board

Date: 2<sup>nd</sup> November 2011

### Subject: Waste Solution for Leeds – Residual Waste Treatment PFI Project

Are specific electoral Wards affected? If relevant, name(s) of Ward(s): ALL	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Is the decision eligible for Call-In?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number:  Appendices B and C are Exempt / Confidential under access to Information Procedure Rule 10.4 (3) as they contain information that is commercially sensitive relating to the Council's ongoing waste PFI procurement and the financial and business affairs of Bidders, where the benefit of keeping the information confidential is considered greater than that of allowing public access to the information.  Appendix C will be tabled at the Executive board meeting due to its confidential nature and is therefore excluded from the agenda pack.	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No

### Summary of main issues

1. The report provides Members with an update on the progress of the Residual Waste Treatment PFI project (the "Project") since the last Executive Board update at the Detailed Solution Stage in February 2010. In particular, the report advises on the outcome of the evaluation of tenders received in respect of the Project.
2. The report describes the outcome of the evaluation, identifies the proposed preferred bidder and requests authority to proceed to the Preferred Bidder stage.
3. This report also describes the programme and issues going forward into the preferred bidder and post contract signature stages.

### Recommendations

1. The report recommends that Executive Board:
  - 1.1. Note the contents of this report, including its appendices;

- 1.2. Note the revised cost of “do nothing”;
- 1.3. Note the outcome of the evaluation of tenders; and
- 1.4. Authorise proceeding to the Preferred Bidder Stage, including formal appointment of the preferred bidder.

## **2. Purpose of this report**

2.1. The purpose of this report is to:

- (a) Inform Members of the progress of the Residual Waste Treatment PFI Project since the Executive Board paper in February 2010;
- (b) Inform Members of the outcome of the evaluation process undertaken in respect of the tenders received for the Project;
- (c) Provide an outline of the proposed communications strategy for the next phase of the procurement process; and
- (d) Update Members on the Project revised cost of “do nothing”.

## **3. Background Information**

3.1. The Project has been developed in response to the need to move away from the current reliance on landfilling for residual municipal waste due to its environmental impact and associated financial implications. The Landfill Tax will reach a minimum of £80 per tonne by 2014 making the cost of continued reliance on landfill unsustainable. The Integrated Waste Strategy for Leeds and subsequent updates include the following key targets:

- To achieve a combined recycling and composting rate of greater than 50% of household waste by 2020;
- To recover value from 90% of all household waste by 2020.

3.2. The Project provides a substantial contribution to the City’s household waste recycling performance, and is fundamental to the achievement of the recovery target and the associated reduction in landfill.

3.3. In July 2008 the Executive Board authorised officers to commence procurement of the Project in the Official Journal of The European Union (the OJEU notice). The OJEU notice was published on Wednesday 30th July 2008. Following such publication and receipt of expression of interest, a pre-qualification (PQQ) stage was undertaken. Thirteen bidders participated in this project stage, and evaluation of the PQQ submissions subsequently reduced these to ten bidders who progressed to being invited to participate in dialogue with the City Council.

3.4. The procurement was neutral in respect of the location of any facility and the technology to be used. The City Council carried out a site selection study prior to the commencement of the procurement. This identified the former wholesale market site, owned by the City Council, and other sites which may be appropriate. The initial bids received proposed a number of sites, including the market site, and a range of technology solutions. The suitability of any site and technology proposed was considered as part of the published evaluation criteria.

- 3.5. The evaluation methodology as approved by Executive Board in November 2008 has been used through each procurement stage.
- 3.6. The Invitation to Submit Outline Solutions (ISOS) was issued to bidders on 13th November 2008 as the initial stage of the competitive dialogue procurement and bids were returned on 21st January 2009. Nine bidders offering a wide range of technology solutions, submitted proposals at this bid stage and these were subsequently reduced to four bidders following evaluation of the bids received and the withdrawal of one of the bidders prior to the finalisation of the evaluation.
- 3.7. The Invitation to Submit Detailed Solutions (ISDS) was issued to bidders on 24th June 2009 and bids were returned on 21st October 2009. Four bidders participated in this bid stage and these were subsequently reduced to two bidders following evaluation of the bids received and the withdrawal of one of the bidders before submitting a bid. The decision in respect of the two bidders to progress to the ISRS stage was reported to the Executive Board in February 2010.
- 3.8. The Invitation to Submit Refined Solutions (ISRS) was issued to bidders on 4<sup>th</sup> June 2010 and bids were returned in September 2010. The following table lists the two bidders that participated at the Invitation to Submit Refined Solutions (ISRS) stage:

<b>Consortia</b>	
Aire Valley Environmental, a joint venture between Covanta Energy Ltd and Kelda Water Services Ltd.	
Veolia ES Aurora Limited	

- 3.9. Following a Central Government review of the commercial positions the bidders had adopted, tenders were requested from both remaining bidders.
- 3.10. Tenders were received back on 15<sup>th</sup> July 2011. The evaluation of tenders was undertaken using a series of subgroups that analysed each aspect of the submissions in accordance with the evaluation methodology. The subgroups raised a small number of minor clarification questions regarding consistency issues with each bidder to ensure that the tenders were fully understood and that scores were assessed objectively based upon clear information.
- 3.11. The evaluation methodology approved by the Executive Board in November 2008 considers a range of factors. These are:

<b>Criteria</b>	<b>% Score Allocated</b>
Quality Score	60%
Price Score	40%
<b>Total</b>	<b>100%</b>

<b>Quality Criteria</b>	<b>Allocation</b>
Sustainability	36%
Bid Integrity	4.5%
Commercial and legal	9%
Finance and Corporate Structure	6%
Payment mechanism	4.5%
<b>Total</b>	<b>60%</b>

3.12. The evaluation concluded that the most advantageous tender was submitted by Veolia ES Aurora Ltd (“Veolia”) and it is therefore recommended that Veolia be taken forward to the preferred bidder stage.

3.13. Veolia scored better than the rival bid in both the price and the quality assessment. Further details regarding the evaluation are contained in the confidential Appendices B and C.

3.14. The results of the evaluation were reported to the Residual Waste PFI Project Board at its meeting on 19th September 2011 at which the outcome of the evaluation was confirmed and recommended for approval by the Director of Environment and Neighbourhoods (the “Director”). The Director has subsequently approved the outcome of the evaluation under the Governance framework for PFI/PPP projects and powers delegated under Part 3E of the City Council’s constitution (Officer Delegation Scheme (Executive Functions)).

3.15. Key data regarding the proposed preferred bidder’s solution is provided below:

<b>Bidder Name</b>	Veolia ES Aurora Ltd
<b>Site</b>	Former wholesale market site on Pontefract Lane, Cross Green (drawings showing the exact site location and facility design are attached at <b>Appendix A</b> ).
<b>Capacity</b>	Approximately 183,000 tpa (including ERF capacity of 162,000tpa)
<b>Funding</b>	Corporate Finance - bidder finances the Project from its own balance sheet
<b>Technology</b>	Mechanical pre-treatment to extract recyclates followed by incineration with energy recovery process.
<b>Use of Third Party waste</b>	Third party waste from the Leeds area will be used to maintain plant inputs if City Council waste volumes do not fill the entire capacity.
<b>Maximum height of building</b>	Approximately 40m. with chimney approximately 65m. Appendix A contains artists impressions of the building together with a plan of the site.
<b>Recycling Level</b>	Minimum 10% of the municipal waste input to the facility. This is in addition to the City Council's existing and future recycling from kerbside collections and household waste sorting sites bring banks etc .
<b>Products</b>	The plant will generate a significant amount of electricity, and the income that this generates is used to reduce the price which the

	City Council pays. A significant level of recyclates will be extracted and sent for further reprocessing. Ash created by the incineration process will be treated off site and recycled for use as aggregates. Residues from the treatment of flue gasses (equal to 3.5% of the input waste) will be sent to a special long-term storage/disposal facility.
<b>Emissions</b>	The technology will be fully compliant with the Waste Incineration Directive (WID). The emission standards to be applied will be approved as part of the environmental permit for the facility Issued by the Environment Agency prior to the plant becoming operational.
<b>Minimum Tonnage</b>	The Contract will contain a requirement for the City Council to pay for the processing of 120,000 tonnes of waste per year. The City Council has undertaken scenario testing assuming very high recycling and low housing growth and this 120,000 tonnes per year figure still remains below the level of residual waste that could be expected. In addition the City Council has control over other residual waste stream not included within projections that could be treated at the facility. The PFI contract will also include a requirement on Veolia to obtain commercial waste in Leeds to fill any shortfall and to minimise any cost to the City Council in the event of municipal waste falling below this minimum tonnage. This ensures flexibility and that recycling is not constrained.

#### 4. Main issues

##### 4.1. Having concluded the evaluation of the tenders

- a) A draft of the Pre-Preferred Bidder Final Business Case (PPB FBC) has been submitted to WIDP (based on Veolia's tender) for approval (this is expected to be received prior to Executive Board); and
- b) The Project Team is seeking approval from Executive Board to proceed to preferred bidder and commence the finalisation of the Contract.

##### 4.2. Full detail of the Project timetable to date, and proposed timetable through to Service Commencement is indicated below:

<b>Milestone</b>	<b>Date</b>
Residual Waste OBC approved by WIDP	April 2008
<b>Pre-qualification</b>	
OJEU notice published	July 2008
PQQ submissions	September 2008
Long-list confirmed (10 Bidders)	October 2008
<b>Invitation to Participate in Dialogue</b>	
ISOS documents issued	November 2008
ISOS submissions received	January 2009
Short-list confirmed (4 Bidders)	March 2009
<b>Invitation to Continue Dialogue</b>	
ISDS documents issued	June 2009

ISDS submissions received	October 2009	
Short-list confirmed (2 Bidders)	February 2010	
<b>Invitation to Submit Refined Solutions</b>		
ISRS documents issued	June 2010	
ISRS submission received	September 2010	
Call for Final Tenders (2 Bidders)	July 2011	
Final Tenders received	July 2011	
Final Tender Evaluation completed	September 2011	
<b>Preferred Bidder Stage</b>		<b>Decision Maker</b>
City Council support for proceeding to Preferred Bidder stage	November 2011	Executive Board
Central Government support for proceeding to Preferred Bidder stage (approval of draft PPB FBC)	November 2011	DEFRA (via WIDP)
Authority to contract with Preferred Bidder and approval of submission of the FBC	May 2012	Executive Board
Final approval of project funding (approval of FBC)	June 2012	DEFRA
Contract finalisation and award	June 2012	Director of Environment and Neighbourhoods (under delegated powers)
<b>Post Contract Award Stage</b>		
Planning permission	Spring 2013	Plans panel
Construction Commencement	June 2013	N/A
Service Commencement	Early 2016	N/A

## 5. Corporate Considerations

### 5.1. Consultation and Engagement

5.1.1 Community and stakeholder engagement have been an integral part of the City Council's Residual Waste Treatment Project. The communications programme has been targeted primarily at local Ward Members, local MPs, local businesses and residents within one mile of the proposed RWT sites (approximately 12000), however there have been opportunities for residents city wide to become involved. The programme has been delivered through various means at different times, and included press releases, briefing sessions, drop-in sessions, distribution of information leaflets regular attendance at community meetings City Council's website. The programme has been an iterative process, where new information has been provided to address issues raised previously.

5.1.2 Following the notification of the Preferred Bidder and prior to Veolia initiating their own pre-planning consultations, the City Council's Waste Strategy team and Veolia are setting up a Communications Working Group

to discuss and resolve items such as knowledge sharing, exhibition venues, protocols for finalising consultation materials and the role of City Council officers.

5.1.3 Veolia will undertake their own consultation activities to ensure that Local Ward Members, the general public and other relevant stakeholders are able to be involved in the planning process, and are able to examine and influence the detailed proposals. Information will be provided to local communities on the detailed proposals by mail shots, a dedicated web page, public exhibitions and/or question and answer sessions at locations convenient for the communities and businesses closest to the proposed Facility. Veolia's consultation activities are expected to be between November and the end of February, with the planning application submitted in spring 2012.

5.1.4 In addition, Veolia will set up a Community Liaison Panel comprising representatives from a broad spectrum of community interests. Its members may be drawn from the database of residents who have previously expressed an interest in the Project. The members of the Panel will provide independent points of contact for community members to discuss issues and pass on their comments to Veolia. The Panel will meet at regular intervals throughout the lifetime of the Project, including during the construction and operational phases.

## **5.2 Equality and Diversity / Cohesion and Integration**

5.2.1 An Equality Impact Assessment has been carried out on the Project and the successful tender meets the requirements identified in the assessment process.

## **5.3 Council Policies and City Priorities**

5.3.1 In 2006, the City Council adopted its Integrated Waste Strategy for Leeds. In addition to waste prevention objectives, the Integrated Waste Strategy for Leeds describes how Government targets for recycling and reducing waste sent to landfill will be met by the City Council. Since the strategy was adopted significant progress in improving waste collection services in Leeds has been made including:

- introduction of garden waste collections to over 190,000 properties;
- piloting weekly food waste collections; and
- closing out remaining gaps in the city-wide provision of kerbside recycling services.

5.3.2 The recycling rate in Leeds has continued to increase from 23.0% in 2006/7 to 34.7% in 2010-11. The City Council's current year's (2011/2012) performance to date (for April, May and June 2011) has been in excess of 40%. The City Council is on target to reach its target of recycling in excess of 50% of household waste by 2020.



5.3.3 However, the need for a solution to divert the remaining residual waste from landfill remains a clear priority, and the cost of disposing of this waste increases each year, with Landfill Tax rising to £80 per tonne by 2014.

5.3.4 The focus of the Project is to provide residual waste treatment infrastructure required to ensure that the City Council increases recycling, meets its targets for the recovery of value from waste and diverts the necessary level of waste from landfill. The development of this infrastructure represents a radical change in terms of how Leeds' waste is managed and will deliver a major reduction in the impact of this waste on the environment.

## **5.4 Resources and Value for Money**

### **5.4.1 Price Ceiling ("Do Nothing Scenario")**

5.4.1.1 The price ceiling for the Project (the "Price Ceiling") has been set with reference to the cost of continuing to landfill residual waste (the "do nothing scenario"). The "do nothing scenario" cost was last reported to Executive Board in February 2010. This was based on a set of assumptions which have now been updated, and consequently the latest position in respect of the core assumptions underpinning the "do nothing scenario" are set out below:

- An overall decrease in waste flows based on information available in March 2011;
- A forecast operational period for the Residual Waste Treatment facility from 1<sup>st</sup> March 2016 to 28<sup>th</sup> February 2041, which is a delay on the anticipated service period;
- Landfill Tax per tonne rising from £72 per tonne to £80 per tonne in 2014/15 (as specified by the Chancellor in the 2010 Budget), with assumption that landfill tax will remain at this level in real terms going forward. Therefore an increase of 2.5% per annum has been assumed to reflect inflation throughout the Contract Period;
- Landfill gatefee per tonne based on March 2011 costs and indexed in line with current expectations; and
- The removal of LATS from 2013/14 as a result of the Government announcement to abolish the scheme at the end of 2012/13 (previously included at £50 per tonne).

5.4.1.2 The table below sets out the current cost of the "do nothing scenario" compared to the position previously reported to Executive Board:

Table 1: Previous Executive Board Approval (February 2010) and current cost of the “do nothing scenario”.

	‘Do Nothing’ Scenario (previously approved at Feb 2010 Executive Board) £000s	Current “do nothing scenario”  £000s	Movement between Previous ‘do nothing’ and current ‘do nothing’ £000s
<b>Price Ceiling (2010 to 2041 (Contract Expiry Date))</b>	<b>633,101</b>	<b>755,453</b>	<b>122,352</b>
Less: Cost of disposal between 2010 - 2015	(59,556)	(94,552)	(34,996)
<b>Cost of ‘Do Nothing’ to the City Council during the Contract Period (2016 to 2041)</b>	<b>573,545</b>	<b>660,901</b>	<b>87,356</b>

- 5.4.1.3 Both tenders received are significantly lower than the “do nothing scenario” cost reported to Executive Board in February 2010, and are consequently well within the current cost of the “do nothing scenario”.

The current cost of ‘do nothing’ during the Contract Period is £661m and the Bidder’s solution was just under £200m lower than the cost of ‘do nothing’ to the City Council during the Contract Period (2016 to 2041).

- 5.4.1.4 As part of its sensitivity analysis, the City Council has considered the assumptions which could potentially lead to a change in the price of the Project and these are outlined below:
- A delay to the Planning Approval date (beyond the 12 months included within the current programme). The Contract is expected to be signed prior to the planning permission being granted, and the risk of price increases, arising as a result of consequent delays to planning permission being granted remains with the City Council;
  - A change to the Foreign Exchange rate assumed in the tender. Approximately 40% of the capital costs of the Project will need to be paid for in Euros, as some of the equipment is purchased from Europe. Therefore, there remains a risk to the Project (and the City Council) that the cost of the capital works could change as the foreign exchange rate fluctuates.
  - Changes to the City Council’s forecast Wasteflow model;
  - Changes to the NNDR estimate (which is treated as a pass through cost); and

- A delay to the Financial Close date beyond the Fixed Price Bid Validity period (30th September 2012).
- 5.4.1.5 It should be noted that these price change scenarios are not exclusive to the successful tender, and would have a similar impact on both tenders.
- 5.4.1.6 The most significant of these price risks to the Project are considered to be a delay to the Planning Approval date, a change to the Foreign Exchange rate issued to Bidders at Final Tender or a combination of the above scenarios.
- 5.4.1.7 However, as a result of the Preferred Bidder's solution being significantly lower than the City Council's Price Ceiling, the City Council is confident that even in these worst case price change scenarios it has sufficient headroom to absorb these costs without exceeding the Price Ceiling. In addition, the City Council has yet to determine its Foreign Exchange rate hedging strategy, which could lead to the purchase of an option by Veolia which could mitigate some of the potential exposure to price changes from Foreign Exchange rates. This is to be determined during the Preferred Bidder stage and the position will be updated and included with the Project's FBC.

## **5.5 Legal Implications, Access to Information and Call In**

- 5.5.1 Appendices B and C to this report contain exempt information under Access to Information Rule 10.4 (3) as they contain commercially sensitive information on the City Council's approach to procurement issues, and commercially sensitive pricing and information about the commercial risk position of bidders, where the benefit of keeping the information confidential is considered greater than that of allowing public access to the information.
- 5.5.2 As this is an Executive Board decision, the subject of this report is open to Call In.

## **5.6 Risk Management**

- 5.6.1 As with any project of this scale, there are a number of issues and risks to be managed in moving towards contract close. The main risks at this point relate to obtaining planning permission for the facility.
- 5.6.2 Further risks that may arise in relation to the programme are:
- i. Planning issues leading to Project Implementation delayed and negative cost implications.

Countermeasure: Ensure early engagement with Planners to ensure that site surveys are undertaken early with in the process.

- ii. Foreign exchange rate risk giving rise to changing capital expenditure costs throughout the procurement.

Countermeasure: Continual monitoring of relevant exchange rates. Project financial advisor has reviewed the hedging strategy. The proposed Preferred Bidder is well within the affordability ceiling with headroom for any potential foreign exchange rate increases.

- iii. Schedule 2 of the Controlled Waste Regulations 1992<sup>1</sup> could lead to an increase in the volume of waste the City Council collects in the future. Waste currently defined as commercial (i.e. prison and hospital waste) may need to be collected.

Countermeasure: There is an element of commercial waste capacity within the solution. The commercial waste could be replaced by additional City Council waste which would allow the City Council flexibility if this scenario were to arise.

- iv. The City Council may be asked to make Architectural Enhancements as a result of the planning process which may lead to increased costs to the Project.

Countermeasure: Ensure early liaison with Planners about possible site constraints. Work to be undertaken at the Preferred Bidder stage with Veolia through the Sites and Planning meetings in partnership with Planners to minimise risk.

- v. Permit approval requires alteration to design and a delay to the Project.

Countermeasure: Veolia has agreed to take all financial risk in this regard and there is a delay long stop.

## 6. Conclusions

- a) The Project will secure significant capital investment and contribute significantly to the City Council's Integrated Waste strategy for Leeds 2005 – 2035, therefore contributing to achieving landfill diversion targets and Leeds City Council's Climate Change strategy.
- b) The procurement is nearing completion and requires approval of a draft Final Business Case (FBC) by WIDP. Work to obtain this approval has been ongoing and it is anticipated that it will be received prior to the Executive Board meeting.
- c) The Project remains affordable in the context of the price ceiling approved by Executive Board in February 2010 and the updated cost of the "do nothing scenario" detailed in paragraph 4.4 of this report. The few financial assumptions which may impact upon the Project costs are not anticipated to cause the Project to exceed the Price Ceiling and would not therefore prevent the Project from proceeding to financial close.

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<sup>1</sup> <http://www.legislation.gov.uk/ukxi/1992/588/schedule/2/made>

- d) Progression to Preferred Bidder and later Financial Close and contract signature will enable commencement of the planning process followed by commencement of the Project which will bring over £140million of capital investment to assist the City Council in complying with its legal requirements and strategic objectives in respect of Leeds' household waste.

## **7. Recommendations**

### **7.1 Members of the Executive Board are recommended to:**

- a) Note the contents of this report, including its appendices;
- b) Note the revised price ceiling;
- c) Note the outcome of the evaluation of tenders; and
- d) Authorise proceeding to the Preferred Bidder Stage, including formal appointment of the preferred bidder.

## **8 Background documents**

1. Report of the Director Environment and Neighbourhoods to Executive Board, 14th November 2007: "Waste Solution for Leeds – Submission of the Outline Business Case for the Residual Waste Treatment Project".
2. Report of the Director Environment and Neighbourhoods to Executive Board, 16th July 2008: "Waste Solution for Leeds – Residual Waste Treatment PFI project - Evaluation Methodology and Update"
3. Report of the Director Environment and Neighbourhoods to Executive Board 5th November 2008: "Waste Solution for Leeds – Residual Waste Treatment PFI Project - Evaluation Methodology and Update"
4. Report of the Director Environment and Neighbourhoods to Executive Board, 12<sup>th</sup> February 2010: "Waste Solution for Leeds – Residual Waste Treatment PFI Project – Results of Detailed Solutions Stage"