Executive Report

Milton Keynes City Council

Cabinet Report – 7 November 2023

MILTON KEYNES WASTE RECOVERY PARK – FUTURE OPTIONS FOR THE OPERATIONAL DELIVERY OF THE PLANT

Name of Cabinet Member	**Councillor Rob Middleton** Cabinet Member for Resources **Councillor Lauren Townsend** Cabinet Member for Public Realm
Report sponsor	**Stuart Proffitt** Director Environment and Property
Report author	**Nicholas Hannon** Head of Environment and Waste Services nicholas.hannon@milton-keynes.gov.uk 01908 252577

Exempt / confidential / not for publication	**Yes – all annexes (A to G)**
Council Plan reference	**N/A**
Wards affected	**All wards**

Executive summary

This report outlines an investment programme and an enhanced operational position for the Milton Keynes Waste Recovery Park (MKWRP), based on a varied contractual relationship between MKCC (as the plant's owners) and Thalia and Ferrovial (the current operators). The Authority will continue to benefit from the asset over the contracted term. The position arising from this decision will provide greater security of sustained service provision, service retention and continuity and an improved financial position for the Authority.

1. Proposed Decisions

1.1 That the variation of the contract for the Residual Waste Treatment Facility as summarsed in section 3 (Implications of the Decision) of this report, be progressed.

1.2 That authority be delegated to the Director Environment and Property, in consultation with the Director Finance and Resources (s151), the Director Law of Governance (Monitoring Officer), as well as the Cabinet Member for Resources and Innovation and / or the Cabinet Member for Public Realm to:

a) agree non-material amendments to the proposed Deed of Variation (**exempt Annex A**); and

b) finalise and enter into the Deed of Variation and any other necessary formal documents to effect the agreed position.

1.3 That the Cabinet note and endorse the outcomes of continued work to deliver these key points:

- Owning the asset outright;
- Ongoing and sustained provision of £0 per tonne gate fee;
- Increased recycling rates; and
- Significantly reduced landfill rates

2. Why is the decision needed?

2.1 Milton Keynes Waste Recovery Park (MKWRP) is critical asset in ownership of the Authority providing significant, financial, and service benefits, over a sustained period. The original business case is provided in exempt Annex B – MKWRP Five Year Plan.

2.2 Since 2018 Milton Keynes City Council has worked to deliver the UK's first working gasification plant. Over the past 12 months we have seen strong operational performance and availability of a key asset known as the 'Advanced Thermal Treatment' (ATT) facility. This is referenced and expanded upon in exempt Annex B – MKWRP Five Year Plan. Delivering performance of an asset of this level is a positive and notable achievement, particularly given that recent availability figures indicate some other plants in the UK are not operational.

2.3 The plant itself is a source of civic pride, providing electricity up to an equivalent of 11,000 homes, powering one third of the environmental services fleet via a private wire, disposing of waste produced in Milton Keynes within the boundaries of the city and was referred to in the application for City Status.

2.4 Whilst the Authority owns the asset, a contractor has been procured to deliver 15-year operations with zero gate fee which has insulated the Authority and the taxpayer from wider market pressures for waste disposal. It has also provided flexibility and operational availability for waste collections.

2.5 Over the past three years the waste market has hardened, whilst acquisitions and mergers have risen, further reducing competition. Locally this meant that in October 2022 MKWRP operator Amey was sold to One Equity Partners and Buckthorn Partners. This led to the creation of a separate company called Thalia, which comprises of Amey's former waste treatment division and remains wholly owned by parent company Ferrovial. More detail on the financial position of the contract with Thalia is provided in exempt Annex B – MKWRP Five Year Plan.

2.6 Maintaining the asset to the strong performance denoted in exempt Annex B is challenging and more expensive than was profiled in the baseline for equipment replacement and maintenance costs provided for in the contract. This has created a long-term financial deficiency within the operational costs of the contract.

2.7 The original business case outlined that the waste disposal budget would be used to repay the £129M capital sum of the facility. This is currently being realised financially. However, maintaining the current £0/tonne gate fee is a tactical priority for the Authority. This is a core driver for the investment strategy, reprofiled risk approach and revenue remediation approach, by effectively ensuring contractual security and service delivery.

2.8 Furthermore, the security of service provision at MKWRP is even more imperative beyond that of waste disposal. The Environmental Services Contract provides electricity via private wire to our landscaping, street cleansing and internal fleets. As part of phase 2 this is likely to expand to our Refuse Collection Vehicle fleet. The facility may be utilised for heat provision in the future to residents and businesses in Milton Keynes and this is currently under review.

2.9 A Deed of Variation to the contract has been negotiated which provides for asset investment, reprofiled risk approach and revenue remediation from the Authority and offsets some major commercial and service delivery risks that in their absence would have created. This in return yields an improved securities package for the Authority albeit over a shorter delivery period.

2.10 A significant change for all parties is the shortening of the contractual term to end of March 2026, from end March 2033, with a provision for a mutually agreed extension to end of March 2028, should it be required for the Authority. This shortens the original contract from a 15-year delivery period to 10 years.

2.11 The negotiations held with Thalia and Ferrovial have continued to be productive, and the key commercial positions are agreed. These are captured in detail in Annex A – Draft Deed of Variation.

2.12 As part of these proposals to rebalance the contractual position it is intended that a future Deed of Variation will be presented which proposes for the Local Authority to potentially purchase the electricity produced by MKWRP for its estate and asset base. It is profiled that revenue spend outlined in section 3 a) will marginally outset by the surety and savings provided by this proposal.

3. Implications of the decision

Financial	Y	Human rights, equalities, diversity	N
Legal	Y	Policies or Council Plan	Y
Communication	N	Procurement	Y
Energy Efficiency	Y	Workforce	N

a) Financial implications

In approving the consolidation and transition of the contract the Council is, in summary, agreeing to:

- finance an initial capital investment for up to three-years
- reprofile the revenue spent on the contract to be on market with what MKCC would expect to pay even when owning the facility;
- reflect new legislative provisions around Persistent Organic Pollutants (POPs) requiring material to be shredded at the Waste Transfer Station by the Recycling Contractor and disposed of at MKWRP (necessitating capital investment to enable direct shredding of material into the bunker.

Both commercial financial implications are provided and detailed in confidential Annex B – MKWRP Five Year Plan.

b) Legal implications

Variation of the contract for the Residual Waste Treatment Facility engages procurement law principles and requires consideration of application of subsidy control provisions under the Subsidy Control Act 2022 (the Act). Legal advice from experts in this area has been sought externally and governance of the variation included a monthly Board meeting comprising the Council's s151 Officer, Monitoring Officer, and the Director Environment and Property who made decisions informed by papers and advice from external solicitors and the Council's legal, financial, and service teams. Legal advice notes relating to procurement and subsidy control are provided in exempt Annex G and exempt Annex C which set out a full analysis of the relevant legal issues.

Recognising that this is not a straightforward exercise and applying a risk-based approach, the summary position is that there is an arguable case that the proposed variation does not constitute a subsidy under the UK's applicable subsidy control rules. A key mitigant in respect of subsidy risk is that the Council is taking reasonable steps in the way that a reasonable market operator might. As the Act is relatively new and untested in some areas, it was prudent to take the legal analysis and consider if the variation amounted to a subsidy whether it would be lawful subsidy if it was found that the variations amounted to a subsidy. It is considered that if a subsidy is found to arise the Council has an arguable case that it is lawful. This is based on the longstanding market failures in the gasification market and the way that the Council has tailored the deed of variation to the minimum payments/changes to the tendered contract necessary to ensure the plant is in the best position to be re-tendered in or around 2026. The fact that the Council is tendering the operations and maintenance of the plant in the future provides a further mitigant to potential challenge. The subsidy control table will be completed and submitted at the end of the call-in period for this decision.

To provide additional security, the Council has agreed a position for this Deed of Variation (DoV) which will ensure that Ferrovial is the principal obligor for the £5M Parent Company Guarantee. This legal documentation is provided in confidential Annex F. This should increase to £10M pending the outcome of a Delegated Decision and further DoV planned for January 2024.

c) Procurement implications

Variation of the contract for the Residual Waste Treatment Facility engages procurement law principles and requires consideration of subsidy control provisions under the Subsidy Control Act 2022 (the Act). The legal advice provided for Regulation 72 of the Public Contracts Regulations 2015 is expanded upon in exempt Annex G - Regulation 72 Legal Advice Note.

After careful consideration of the legality of this contract change, the Council considers that the changes fall within the safe harbours of Regulation 72 (1) (E).

d) Other implications

Other Implications and risks are provided in exempt Annex B – MKWRP Five Year Plan.

4. Alternatives

4.1 Do nothing

From a purely legal perspective, the risk is with the contractor and any action taken is at additional cost to the Authority. Therefore, one option would be for the contractor to 'take the strain' and procure all additional capital requirements for the plant. This would likely trigger a termination scenario and distressed procurement. Given the prevailing market conditions it is unlikely that the favourable financial terms of the current contract would be reobtained, meaning the Authority would not continue to benefit for the next three – five years.

4.2 Option 1 – Terminate and re-procure

To terminate the contract the Authority would have to have good reason to do so. As referred in this report the asset has performed well, the boiler has been rebuilt and this performance is demonstrated in Annex B – MKWRP Five Year Plan. As such, with a strong performance of the asset and the ongoing delivery of the original financial benefits reasons to terminate for convenience are not immediately evident. The existing financial arrangements within the contract are not sustainable for the incumbent contractor and therefore a re-procurement earlier than the anticipated 2033 is inevitable and hence why the contract has been brought forward to 2026 (with a potential extension to 2028). However, the procurement for MKWRP will take 30 to 36 months to undertake (minimum) inclusive of an 18-month document preparation period. Therefore, this option is not recommended.

4.3 Option 2 – Capital Investment and Revenue Supplementation Programme (without negotiation)

The Authority could pursue an option whereby it funds the Capital Investment Programme and revenue supplementation. However, this option sees a simple pass through of cost for the asset from the contractor through to the Authority. This process will still see a publicly visible procurement on capital investment and the respective business case sign off as well as a contract variation for changing how final disposal costs are handled. This option would mean that the contractor will have reduced losses, and this will demonstrate a highly committed landlord willing to fund capital costs on its asset. This would stabilise the contract by the Authority acting as a backstop to finance capital investment. This would as a result provide increased surety on contractor retention (and therefore avoiding a termination / crashed contract scenario).

However, this must be balanced against the need for best value and advice on subsidy and financial control. This option does not taper the capital investment programme and would not demonstrate best value potentially creating a subsidy control issue. This option would lack the securities that the Authority has secured through negotiation which have manifested themselves through the Annex A – Draft Deed of Variation. Therefore, this option is not recommended.

4.4 Option 3 – Capital Investment Programme with negotiation (Recommended Option)

The current contractor has stabilised the operational performance of the MKWRP asset. There is a risk arising from the sale of Amey that the new delivery vehicle could enter distress if it not financed from its core shareholder which would render a forced termination scenario. Retention of the contractor is a key outcome for a period to enable a public procurement for a new contract while balancing against what is the best financial outcome for the Authority over a five-year period.

This option provides a revised and recalibrated commercial position in what is a fluid delivery market albeit with few market operators but is cognisant that the current contractor is in financial distress and therefore the longevity of the existing financial arrangement is limited.

To maintain the favourable financial conditions of the existing contract the negotiated position delivers on providing:

- comfort on ongoing contractual retention with sufficient time to enable a re-procurement;
- protection sought from the capital investment;
- reprofiled revenue position that is more reflective of what a market cost would be for disposal of waste post processing and encapsulating this in advance of going back out to procurement for the facility; and
- allows the Authority to demonstrate best value available through competitive retendering.

5. Timetable for implementation

5.1 If approval is granted, the Deed of Variation in the draft form outlined in exempt Annex A, and any other necessary formal documents will be finalised and agreed by the Council and the Contractor by end of March 2024.

5.2 It is proposed that if approval is granted that commercial discussions will commence for the second Deed of Variation from November 2023 with a governance approval process for a further Delegated Decision in January 2024 to ensure all necessary formal documents will be finalised and agreed by the Council and the Contractor by end of March 2024.

List of annexes

The annexes are not for publication by virtue of Paragraphs 3 (Information Relating to the Financial or Business Affairs of the Authority) and 5 (Information in respect of which a claim to legal professional privilege could be maintained in legal proceedings) of Part 1 of Schedule 12A of the Local Government Act 1972.

Annex A (Confidential) – Draft Deed of Variation

Annex B (Confidential) – MKWRP Five Year Plan

Annex C (Confidential) – Legal and Subsidy Control Opinion

Annex D (Confidential) – MKWRP Risk Register. Note this will be an open document following it's update and completion of the planned executive decision in January 2024.

Annex E (Confidential) – Subsidy Control Table – Capital and Revenue Profile

Annex F (Confidential) – Replacement Project Agreement Parent Company Guarantee (PCG)

Annex G (Confidential) – Regulation 72 Legal Advice Note

List of background papers

- "Residual Waste Treatment Facility – Deed of Variation Delegated Decision" on 22 February 2018 - Meeting of Delegated Decisions on Thursday 22nd February, 2018, 8.20 pm | Milton Keynes City Council (moderngov.co.uk)
- "MKWRP Commercialisation - Deed of Variation Delegated Decision" on 26 September 2019 - Meeting of Delegated Decisions on Thursday 26th September, 2019, 5.30 pm | Milton Keynes City Council (moderngov.co.uk)
- "Milton Keynes Waste Recovery Park (MKWRP) Capital Programme Delegated Decision" on 31 January 2023 - Agenda for Delegated Decisions on Tuesday 31st January, 2023, 5.30 pm | Milton Keynes City Council (moderngov.co.uk)