

Agenda

Waste Credit Governance Committee

Friday, 24 March 2017, 2.00 pm
County Hall, Worcester

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ਪੰਜਾਬੀ। ਜੇ ਤੁਸੀਂ ਇਸ ਦਸਤਾਵੇਜ਼ ਦਾ ਮਸ਼ਹੂਰ ਸਮਝ ਨਹੀਂ ਸਕਦੇ ਅਤੇ ਕਿਸੇ ਅਜਿਹੇ ਵਿਅਕਤੀ ਤੱਕ ਪਹੁੰਚ ਨਹੀਂ ਹੈ, ਜੋ ਇਸਦਾ ਤੁਹਾਡੇ ਲਈ ਅਨੁਵਾਦ ਕਰ ਸਕੇ, ਤਾਂ ਕਿਰਪਾ ਕਰਕੇ ਮਦਦ ਲਈ 01905 765765 'ਤੇ ਫ਼ੋਨ ਕਰੋ। (Punjabi)

DISCLOSING INTERESTS

There are now 2 types of interests:
'Disclosable pecuniary interests' and **'other disclosable interests'**

WHAT IS A 'DISCLOSABLE PECUNIARY INTEREST' (DPI)?

- Any **employment**, office, trade or vocation carried on for profit or gain
- **Sponsorship** by a 3rd party of your member or election expenses
- Any **contract** for goods, services or works between the Council and you, a firm where you are a partner/director, or company in which you hold shares
- Interests in **land** in Worcestershire (including licence to occupy for a month or longer)
- **Shares** etc (with either a total nominal value above £25,000 or 1% of the total issued share capital) in companies with a place of business or land in Worcestershire.

NB Your DPIs include the interests of your spouse/partner as well as you

WHAT MUST I DO WITH A DPI?

- **Register** it within 28 days and
- **Declare** it where you have a DPI in a matter at a particular meeting
 - you must **not participate** and you **must withdraw**.

NB It is a criminal offence to participate in matters in which you have a DPI

WHAT ABOUT 'OTHER DISCLOSABLE INTERESTS'?

- No need to register them but
- You must **declare** them at a particular meeting where:
You/your family/person or body with whom you are associated have a **pecuniary interest** in or **close connection** with the matter under discussion.

WHAT ABOUT MEMBERSHIP OF ANOTHER AUTHORITY OR PUBLIC BODY?

You will not normally even need to declare this as an interest. The only exception is where the conflict of interest is so significant it is seen as likely to prejudice your judgement of the public interest.

DO I HAVE TO WITHDRAW IF I HAVE A DISCLOSABLE INTEREST WHICH ISN'T A DPI?

Not normally. You must withdraw only if it:

- affects your **pecuniary interests OR** relates to a **planning or regulatory** matter
- **AND** it is seen as likely to **prejudice your judgement** of the public interest.

DON'T FORGET

- If you have a disclosable interest at a meeting you must **disclose both its existence and nature** – 'as noted/recorded' is insufficient
- **Declarations must relate to specific business** on the agenda
 - General scattergun declarations are not needed and achieve little
- Breaches of most of the **DPI provisions** are now **criminal offences** which may be referred to the police which can on conviction by a court lead to fines up to £5,000 and disqualification up to 5 years
- Formal **dispensation** in respect of interests can be sought in appropriate cases.

Waste Credit Governance Committee
Friday, 24 March 2017, 2.00 pm, County Hall, Worcester

Membership: Mr P Grove (Chairman), Mr L C R Mallett (Vice Chairman),
Mr R C Adams, Mrs S Askin, Mr R W Banks, Mr P Denham,
Mr A I Hardman and Mr P A Tuthill

Agenda

Item No	Subject	Page No
1	Apologies and Named Substitutes	
2	Declarations of Interest	
3	Public Participation Members of the public wishing to take part should notify the Head of Legal and Democratic Services in writing or by email indicating the nature and content of their proposed participation no later than 9.00am on the working day before the meeting (in this case 23 March 2017). Further details are available on the Council's website. Enquiries can be made through the telephone number/e-mail below.	
4	Confirmation of Minutes To confirm the Minutes of the meeting held on 13 December 2016. (previously circulated – pink pages)	
5	Actual construction period cash flow test	1 - 14
6	Progress summary from technical advisors	15 - 18
7	Risk Register	19 - 26
8	Waivers/consents	27 - 28

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To obtain further information or a copy of this agenda contact Simon Lewis, Committee Officer on 01905 846621, slewis@worcestershire.gov.uk

All the above reports and supporting information can be accessed via the Council's website

Date of Issue: Thursday, 16 March 2017

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WASTE CREDIT GOVERNANCE COMMITTEE
24 MARCH 2017**ACTUAL CONSTRUCTION PERIOD CASH FLOW TEST**

Recommendation

- 1. The Chief Financial Officer recommends that:**
 - a) The result Actual Construction Period Cash Flow Test be considered.**
 - b) The Committee consider whether to report any matters to Council.**

Introduction

2. The Actual Construction Period Cash Flow Test (ACPCFT) is prepared by Mercia Waste Management on a quarterly basis and reviewed by Deloitte, acting in the capacity as Financial Advisers to the Councils in relation to the Senior Term Loan Facilities Agreement (STFLA), to determine whether:

“Actual Operating Cash generated during that period plus the brought forward cash balance attributable to operations is equal to, or exceeds... the amount of Operating Cash projected to be generated during that period plus the brought forward cash balance attributable to operations as shown in the Base Case Financial Model.”

Review performed by Deloitte

3. In performing the review Deloitte have agreed the terms of the calculation to the STLFA:
 - Agreed the “model” Operating Cash generated during the period to the Base Case Financial Model
 - Agreed the actual Operating Cash generated during the period to management information
 - Re-performed the calculation of the ACPCFT
 - Compared the senior term loan facility drawdowns against those forecast in the Base Case Financial Model.

Summary of Results

4. The result of the ACPCFT performed by Mercia for the period under review is an Excess Cash Flow amount as at 31 December 2016 of £3,186k. The result shows that in the period from 1 May 2014 to 31 December 2016, the operations have produced £3,186k more than was forecast for this period in the Base Case Financial Model.

5. Based on this result the ACPCFT for the period under review is satisfied.

Contact Points

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Supporting Information

- Appendix – Actual Construction Period Cash Flow Test

Background Papers

In the opinion of the proper officer (in this case the Chief Financial Officer) there are no background papers relating to the subject matter of this report.



Senior Term Loan Facility Agreement

Actual Construction Period Cash Flow Test

For the period:
1 October 2016 to 31 December 2016

Important notice

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Actual Construction Period Cash Flow Test

Background

Mercia has a Waste Management Services Contract ("WMSC") with the Councils. Mercia secured planning consent for a new facility and re-negotiated the WMSC for the design, construction and operation of an Energy from Waste ("EfW") plant over the remainder of the WMSC, due to expire in 2023. Financial close was reached in May 2014.

In order to ensure the funding solution demonstrated Value for Money ("VfM"), the Councils used their Prudential borrowing powers to debt fund Mercia's EfW Plant.

Based on a capital structure of 85% debt and 15% equity, the Councils issued a senior loan facility.

Within the Senior Term Loan Facility Agreement ("STLFA"), the Councils included an Actual Construction Period Cash Flow Test ("ACPCFT"). This test is carried out on a quarterly basis following financial close (the first quarter ending 30 September 2014) and is used to determine whether:

"Actual Operating Cash generated during that period plus the brought forward cash balance attributable to operations is equal to, or exceeds... the amount of Operating Cash projected to be generated during that period plus the brought forward cash balance attributable to operations as shown in the Base Case Financial Model."

Should a shortfall occur, Mercia will be required to remedy this shortfall by means of an equity injection equal to the amount of the shortfall in accordance with the contractual documentation.

Mercia operate the local council recycling collections and the landfill site, as well as the construction of the new EfW plant.

Source: Mercia; Financial Model; Senior Term Loan Facility Agreement.

Scope of review

Deloitte has reviewed the calculation provided by Mercia for the ACPCFT. In doing so Deloitte has:

- Agreed the terms of the calculation to the STLFA;
- Agreed the "model" Operating Cash generated during the period to the Base Case Financial Model;
- Agreed the actual Operating Cash generated during the period to management information;
- Re-performed the calculation of the ACPCFT; and
- Compared the senior term loan facility draw downs against those forecast in the Base Case Financial Model.

We have not received any technical reports for the period 1 October 2016 to 31 December 2016.

Summary of results

The result of the ACPCFT performed by Mercia for the period under review is an Excess Cash Flow amount as at 31 December 2016 of £3,186k, which has increased by £2,135k from the Cash Flow flow test in the previous period.

This shows that from 1 May 2014 to 31 December 2016, the operations have produced £3,186k more than was forecast in the Base Case Financial Model, which is a further increase in Excess Cash Flow from Q1 2016, following four consecutive periods of under-performance against the modelled forecast, up to and including Q4 2015.

Based on the above, the ACPCFT for the quarterly period under review would be satisfied. In completing our work set out above, we have not identified any inconsistencies between Mercia's calculation and the underlying information.

Calculation

Actual Construction Period Cash Flow Test

Metric (£000)	May – Sep 14	Oct – Dec 14	Jan - Mar 15	Apr - Jun 15	Jul - Sep 15	Oct - Dec 15	Jan - Mar 16	Apr - Jun 16	Jul - Sep 16	Sep - Dec 16
Base case financial model										
<i>b/f cash attributable to Ops</i>	4,254	4,793	7,051	9,123	11,246	13,203	15,388	17,482	19,801	22,115
Gross revenue	18,603	10,448	10,847	11,813	12,374	10,627	11,140	12,046	12,640	10,861
Operating costs	(14,893)	(8,111)	(8,320)	(8,961)	(9,253)	(8,590)	(8,821)	(9,439)	(9,671)	(8,775)
Changes in working capital	(1,212)	320	(18)	(252)	(37)	451	138	134	(216)	359
Cell preparation assets	(612)	0	0	0	(632)	0	0	0	0	0
Corporation tax	(1,346)	(400)	(437)	(477)	(494)	(303)	(363)	(423)	(439)	(318)
Total change	539	2,258	2,072	2,122	1,957	2,185	2,094	2,319	2,314	2,127
<i>c/f cash attributable to Ops</i>	4,793	7,051	9,123	11,246	13,203	15,388	17,482	19,801	22,115	24,242
Actuals										
<i>b/f cash attributable to Ops</i>	4,637	6,480	11,674	10,423	12,333	14,218	15,655	17,860	20,197	23,165
<i>Gross revenue</i>	19,688	13,341	10,578	11,929	12,091	10,523	11,091	13,078	12,487	8,991
Operating costs	(15,557)	(8,588)	(8,509)	(9,372)	(9,682)	(8,916)	(9,245)	(9,812)	(9,847)	(6,409)
Changes in working capital	(1,392)	1,363	(3,018)	(171)	(131)	(341)	358	(928)	332	1,683
Cell preparation assets	(333)	(286)	0	0	(189)	0	0	0	0	0
Corporation tax	(563)	(636)	(302)	(476)	(204)	171	0	0	(4)	(3)
Total change	1,843	5,194	(1,252)	1,910	1,885	1,437	2,204	2,338	2,968	4,262
<i>c/f cash attributable to Ops</i>	6,480	11,674	10,423	12,333	14,218	15,655	17,860	20,197	23,165	27,428
Variance	1,304	2,936	(3,324)	(212)	(72)	(748)	110	20	654	2,135
Excess cash flow a/c b/f	383	1,687	4,623	1,299	1,087	1,015	267	377	396	1,050
Excess cash flow a/c c/f	1,687	4,623	1,299	1,087	1,015	267	377	397	1,050	3,186

Commentary

Summary

- The calculation is the result of a methodology agreed between parties (the Councils and Mercia) as per the STLFA signed on 21 May 2014.
- The outcome of the ACPCFT performed by Mercia for the quarter under review is an Excess Cash Flow amount of £3,186k.
- In the period from 1 May 2014 to 31 December 2016, the operations have produced £3,186k more Excess Cash Flow than was forecast for this period in the Base Case Financial Model.
- We note that in the period there has been an over performance against the Base Case Financial Model of £2,135k, following four consecutive periods of under-performance against the modelled forecast up to and including Q4 2015.
- Based on the above, the ACPCFT for the period under review is satisfied. We have not identified any inconsistencies between Mercia's calculation and the underlying information.
- Following four consecutive quarterly periods of under-performance against the modelled forecast, it has been noted that there has now been four successive quarters of over-performance, with an increase in Excess Cash Flow of £2,135k in Q4 2016 following an increase of £654k in the previous quarter.
- Despite revenue falling short of expectation by £1,869k (£8,991k vs. £10,861k), that was more than made up for by positive performance in both operating costs (£2,366k below expectations) and favourable working capital movements (£1,324k better than expectations). Corporation tax has also performed better than expected, with a £3k charge comparing favourably to an expected £318k charge. Combined, these have led to the Excess Cash Flow total of £2,135k.
- From a discussion with Mercia on 20 February 2017, the under performance of revenue and lower operating costs reflects a diversion of materials to the EfW site in order to support commissioning activities. This means lower landfill tax, which goes through both the cost (when Mercia pay the tax) and revenue lines (when it is recharged to Mercia's customers).

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Revenue and operating costs down against modelled forecast

- We note that for the quarter under consideration, revenue actuals were 17% below the modelled forecast, and operating costs 27% below the modelled forecast.
- Under performance of revenue has been driven by increasing tonnage being diverted to the EfW plant to support the requisite commissioning activities, which have been ramped up at a greater rate than forecasted.
- The EfW site began commissioning activities in Q3 2016, with minimal volumes diverted from landfill. This continued at a greater level through Q4, and is expected to continue, albeit levelling off, in subsequent quarters. Therefore the depressed revenue and cost lines from landfill will continue into future quarters.

Changes in working capital and corporation tax

- The increase in the Excess Cash Flow amount has been principally driven by favourable movements in Operating Costs and working capital, and the position achieved in respect of corporation tax.
- The favourable movement in working capital in the period is largely a reflection of decreasing trade debtors compared to the modelled forecast (£3,312k vs. £593k), predominantly due to the lack of a landfill tax debtor from customers (see above).
- The favourable position with regards to the Corporation Tax relates to two elements: firstly capitalised interest, which is tax deductible, wasn't forecasted in the model. Secondly, Mercia is adopting a different position on capital allowances, depreciating over a shorter period than was initially forecasted. The second of these elements will balance out over the length of the project.

Commentary (continued)

ACPCFT trend

- It has been noted that whilst the Excess Cash Flow amount is still positive at £3,186k (an increase of £2,135k from the previous period), prior to Q1 2016 there were four consecutive periods of under-performance against the modelled forecast (i.e. a negative variance of actuals against the model).
- Mercia stated that there were no significant movements in the pricing of recyclable materials during the period, though Deloitte has not validated this.
- Equally, the recyclable volumes have continued to hold steady; a trend that is expected to continue. Deloitte has not validated this.
- As a result of these factors, operational improvements and the Deed of Rectification, Mercia is projecting a stable or increased Excess Cash Flow Account for the next quarter.
- In any case, should the ACPCFT be failed in subsequent quarters, the process to resolve this has been extracted and included in Appendix 2.

Senior Term Facility Loan draw downs

Actuals vs Forecast in the Financial Model

The table below shows the actual Senior Term Facility Loan draw downs against those forecast in the financial model.

Model	May - Sep 14	Oct - Dec 14	Jan - Mar 15	Apr - Jun 15	Jul - Sep 15	Oct - Dec 15	Jan - Mar 16	Apr - Jun 16	Jul - Sept 16	Oct - Dec 16	Cumulative
Model											
Facility A	5,241	2,341	1,725	5,633	3,205	4,249	2,355	2,448	861	551	28,609
Facility B	18,898	8,426	6,190	20,288	11,490	15,241	8,382	8,699	2,957	1,832	102,404
Total	24,139	10,767	7,915	25,921	14,695	19,490	10,737	11,147	3,818	2,383	131,013
Actual											
Facility A	4,576	-	1,713	2,375	3,289	4,746	5,180	5,626	-	2,021	29,527
Facility B	16,532	-	6,187	8,581	11,883	17,145	18,715	20,324	-	7,300	106,666
Total	21,108	-	7,900	10,956	15,172	21,891	23,895	25,950	-	9,321	136,193
Difference	(3,031)	(10,767)	(15)	(14,965)	477	2,401	13,158	14,803	(3,818)	6,937	5,180

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Facility A is the amortising loan. Capital repayments begin in the quarter ending 30 June 2017 following the end of the construction period. Facility B is the bullet loan which is forecast to be repaid in the quarter ending 31 December 2023.

From discussions with Mercia management, the lack of a draw down in the quarters 1 October 2014 to 31 December 2014 and 1 July 2016 to 30 September 2016 reflects both a delay in the EfW build (meaning less cash was required for the EfW build) and the lower-than-expected capital expenditure in non-EfW build (meaning that more of the cash can be used on the EfW build). Overall the actual loan drawdowns are still expected to match those forecast in the model.

From discussions with Mercia management, the draw downs against the facilities are higher in Q4 2016 compared to the modelled forecast as a result of timing differences between the programme and the milestones assumed in the model. As such there has been an increase in draw downs compared to the modelled forecasts.

Appendix 1

Mercia's calculation (£000)

	1 Oct 16 to 31 Dec 16 ACTUAL	1 Oct 16 to 31 Dec 16 MODEL
Profit Before Depreciation and Tax	2,582	2,086
Working Capital Movement (Operating)	1,683	359
Corporation Tax (Cash)	-3	-318
Operating Cash Flow	4,262	2,127

Excess Cash Flow

	1 Oct to 31 Dec 2016		
	Actual	Model	Var
Operating Cash Opening Balance	23,166	22,116	1,050
Operating Cash Flow (as above)	4,262	2,127	2,135
Operating Cash Closing Balance	27,428	24,242	3,186

Mercia's cash flow notice

<i>Excess Cash – Opening Balance (Sep 2016)</i>	1,050
<i>Gross Revenue</i>	-1,869
<i>Operating Costs</i>	+2,365
<i>Changes in Working Capital</i>	+1,325
<i>Corporation Tax</i>	+315
<i>Total</i>	+2,136
<i>Excess Cash – Closing Balance (Dec 2016)</i>	3,186

Appendix 2

Extracts from Senior Term Loan Facility Agreement

“Actual Construction Period Cash Flow Test” means the quarterly test to be carried out on each Actual Construction Period Cash Flow Testing Date, in relation to the preceding quarter to determine whether: actual Operating Cash generated during that period plus the brought forward cash balance attributable to operations is equal to, or exceeds the amount of Operating Cash projected to be generated during that period plus the brought forward cash balance attributable to operations as shown in the Base Case Financial Model;

“Actual Construction Period Cash Flow Testing Date” means each Quarter Date following Financial Close, up to and including Completion;

“Actual Construction Period Cash Flow Shortfall” has the meaning given to it in clause 15.9 (Actual Construction Cash Flow Test);

“Actual Construction Period Cash Flow Remedy Amount” means the minimum amount necessary following a failure by the Borrower of the Actual Construction Period Cash Flow Test, to pass such test;

“Actual Construction Period Excess Cash Flow Amount” means the amount of Operating Cash generated in any quarter during the Construction Period which is greater than the amount required to satisfy the Actual Construction Period Cash Flow Test; and

“Base Cash Financial Model” means the computer model, agreed between the Lenders and the Borrower at Financial Close, as amended from time to time by agreement between the Lenders and the Borrower and delivered pursuant to paragraph 11.1 (Part I – Initial Conditions Precedent) of Schedule 3;

“Current Assets” means:

- a) cash held by the Borrower;
- b) any balance on the Debt Service Reserve Account;
- c) any balance on the Maintenance Reserve Account;
- d) any prepayments received;
- e) amounts owed to the Borrower and/or the amounts of any accounts receivable (in each case from trade debtors or HMRC in respect of VAT);
- f) amounts in respect of deferred taxes;
- g) inventory; and
- h) any cell preparation assets.

“Current Liabilities” means:

- a) amounts owed by the Borrower and/or the amounts of any accounts payable (in each case to trade creditors or HMRC in respect of National Insurance and VAT);
- b) the amount of any accruals or provisions made;
- c) the amount of any deferred tax liability;
- d) any cell restoration liabilities;
- e) any aftercare liabilities; and
- f) liabilities in respect of Corporation Tax

Appendix 2 (continued)

Extracts from Senior Term Loan Facility Agreement

“**Gross Revenue**” means, at any Ratio Testing Date and without double counting, the sum of:

- a) operating revenue including the Unitary Payment, any interim service payments (if applicable) and any actual or guaranteed third party income, but excluding, for the avoidance of doubt, the Bullet Payment;
- b) interest earned on all cash accounts (other than the Distribution Account);
- c) damages;
- d) insurance Proceeds to the extent received as compensation for loss of revenue;
- e) income earned on Authorised Investments (other than any Authorised Investments in respect of the Distribution Account, if any);
- f) rebates of Tax actually received or projected to be received in the latest Approved Budget; and
- g) all other income or proceeds of a revenue nature from whatever source;

Assumed in the Approved Financial Model to be receivable by the Borrower in the period commencing with such Ratio Testing Date and terminating on the Final Repayment Date or, in respect of any Ratio Testing Period ended on that Ratio Testing Date, all such revenues actually received during such Ratio Testing Period;

“**Operating Cash**” means:

- a) gross Revenue; less
- b) operating costs; plus or minus
- c) changes in Working Capital; less
- d) corporation Tax.

In each case, in respect of the Financial Year, as reflected in the operating cash flow calculation in the Approved Financial Model;

“**Working Capital**” means Current Assets minus Current Liabilities

“Operating Costs” means, without double counting any of those costs, and including any VAT thereon, costs identified as, or as the case may be, falling within the category of:

- a) costs and expenses of administering, maintaining and operating the Borrower, SWSL and BWL and the Project including, without limitation, all operating costs accrued prior to, or arising after Financial Close relating to the Borrower’s, SWSL’s and BWL’s existing operations under, or related to, the Waste Management Services Contract all costs relating to Environmental Matters and the costs of complying with the requirements of Environmental Laws and the terms and conditions of Environmental Authorisations (together in all cases with any applicable VAT thereon which is irrecoverable VAT);
- b) the costs of insurance premia (other than in relation to insurances covering the construction and commissioning of the Plant) and all property and occupation charges and rates to which the Project may be subject (together in each case with any applicable VAT thereon which is irrecoverable VAT);
- c) sums payable by the Borrower under the terms of the Project Documents to which it is a party, other than in relation to construction and commissioning of the Plant (together with any applicable VAT thereon which is irrecoverable VAT);
- d) taxes payable (excluding VAT other than “output tax” within the meaning of Section 24(2) of the Value Added Tax Act 1994) other than in relation to the construction and commissioning of the Plant;
- e) development costs; and
- f) in all cases, the equivalent lines thereafter in each Approved Budget and each Approved Financial Model.

The Borrower may only withdraw sums from the Excess Cash Flow Account:

- i. to meet Project Costs at any time on or after the Take-Over Date, but prior to Completion; or
- ii. to transfer any amount standing to the credit of Excess Cash Flow Account on Completion to the Distribution Account, provided that no Event of Default is continuing.

Appendix 2 (continued)

Extracts from Senior Term Loan Facility Agreement

Actual Construction Period Cash Flow Test

- a) On each Actual Construction Period Cash Flow Testing Date, the Borrower will provide evidence satisfactory to the Lenders (acting reasonably) that the Actual Construction Period Cash Flow Test has been satisfied.
- b) Where there is a failure by the Borrower to satisfy the Actual Construction Period Cash Flow Test on any Actual Construction Period Cash Flow Testing Date (an "**Actual Construction Period Cash Flow Shortfall**"):
 - i. The Borrower shall serve a Standby Equity Funding Notice on each Shareholder pursuant to clause 4.2 (Standby Equity Funding Notice) of the Equity Agreement and through such notice request that each Shareholder contribute Equity in an amount equal to its Standby Contribution in accordance with clause 4.1 (Provision of Standby Equity) of the Equity Agreement; and
 - ii. in the event that [*Shareholder A*] fails to contribute Equity in accordance with clause 15.10(b)(i) above, the Borrower or the Security Agent shall be entitled to make a claim under the Equity Guarantee ([*Shareholder A*]) for an amount equal to [*Shareholder A's*] Standby Contribution of the Actual Construction Period Cash Flow Remedy Amount within the relevant period that such Equity is required to be paid pursuant to clause 8.1(b) ([*Shareholder A's parent*] Guarantee) of the Equity Agreement.

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WASTE CREDIT GOVERNANCE COMMITTEE 24 MARCH 2017

PROGRESS SUMMARY FROM TECHNICAL ADVISORS

Recommendation

- 1. The Chief Financial Officer recommends that:**
 - a) The summary report from Fichtner Consulting Engineers – Technical Advisors be noted.**
 - b) The Committee consider whether to report any matters to Council.**

Introduction

2. As set out in its Terms of Reference, the Committee will be advised by external financial, technical and legal advisers on behalf of the Council's Section 151 Officer.
3. Fichtner Consulting Engineers have been appointed as technical advisor to the lender during the construction phase of the Energy from Waste plant. The company has produced a summary report up to the 2 March 2017 for consideration by the Committee and this is attached as an Appendix.
4. Members should note that the Lenders Technical Advisor agreed that the EfW Plant has achieved Actual Takeover by Mercia from their EPC Contractor, HZI.

Contact Points

County Council Contact Points

County Council: 01905 763763

Worcestershire Hub: 01905 765765

Specific Contact Points for this report

Sean Pearce – Chief Financial Officer

Tel: 01905 846268

Email: spearce@worcestershire.gov.uk

Supporting Information

- Appendix – Summary report from Fichtner Consulting Engineers – up to 2 March 2017

Background Papers

In the opinion of the proper officer (in this case the Chief Financial Officer) there are no background papers relating to the subject matter of this report.

MEMORANDUM

To:	Mark Forrester	Organisation:	Worcestershire County Council
cc:	Simon Lewis	Organisation:	Worcestershire County Council
From:	Kerry Booth	Our Ref:	S1291-2300-0010KSB
Date:	6 th March 2017	No. of Pages:	2
Subject:	Mercia LTA Construction Progress Summary – March 2017		

1 INTRODUCTION

Mercia Waste Management Limited ("Mercia") is constructing the 200,000 tonnes/year, 18 MWe Mercia EnviRecover EfW Plant in Hartlebury, Worcestershire. Fichtner Consulting Engineers Ltd (Fichtner) has been appointed as lender's technical advisor (LTA) for the construction phase of the plant. This summary memo covers relevant activities and progress based on review of latest available reports from the Owner's Engineer (OE) and Mercia (covering 1st – 31st January 2017) and additional information provided to the LTA team since that date.

2 PROJECT PROGRESS

The facility achieved Take Over on 2nd March 2017, two days after the contractual Take Over date of 28th February 2017. The delay compared to the contractual Take Over date was due to HZI's failure to complete a number of required tasks by 28th February, including demonstration of items on the firefighting cause and effect matrix, building services take over tests, emergency lighting tests, completion of high priority building services observations, and removal of all construction equipment and debris.

3 KEY PROJECT RISKS AND OBSERVATIONS

The Project Manager issued the Take Over certificate with Minor Items which do not materially affect the safe or efficient operation of the works outstanding. Following Take Over, HZI is responsible for closing out these Minor Items. Under the terms of the EPC contract, the Performance Bond remains in place until Acceptance, and after Acceptance a Retention Bond must be in place to provide protection to the Owner against any failure by HZI to rectify these items.

4 FINANCIAL AND COMMERCIAL

The cumulative amount which has been certified to date is £114,473,224.60. The LTA has issued twelve payment certificates to allow drawdown on the senior loan.

As Take Over has been achieved, HZI is eligible to apply for the associated payment milestone under the contract. The LTA has not received a request for certification of this payment.

5 HEALTH AND SAFETY

Health and safety standards have been maintained in recent months. There was an increase in site safety observation reports in January, and HZI was instructed that health and safety should remain the top priority.

One red card was issued in January. The red card related to abusive behaviour and language toward HZI staff by a contractor when they were challenged on not wearing appropriate personal protective equipment on site.

6 PLANNED ACTIVITIES NEXT PERIOD

The following activities are planned from March 2017:

- Completion of drainage works in welfare area (subject to previous Variation Order allowing completion after Take Over);
- Completion of Minor Items;
- Completion of the EPC Performance Tests; and
- Delivery of final documentation.

Yours sincerely
FICHTNER Consulting Engineers Limited



Kerry Booth
Associate Senior Consultant



Phin Eddy
Commercial Director

WASTE CREDIT GOVERNANCE COMMITTEE

24 MARCH 2017

RISK REGISTER

Recommendation

- 1. The Chief Financial Officer recommends that:**
 - a) The open and closed risks set out in the Risk Register be considered.**
 - b) The Committee consider whether to report any matters to Council.**

Introduction

2. As set out in its Terms of Reference, the Committee will need to review the risks being borne as a result of the funding provided by the Council to Mercia and consider whether the risks being borne by the Council, as lender, are reasonable and appropriate having regard to the risks typically assumed by long term senior funders to waste projects in the United Kingdom and best banking practice.
3. A Risk Register was established which set out the unmitigated and mitigated risks associated with the loan arrangements. Now that takeover is complete and all but two of the risks have expired, they have been reclassified into open and closed. The two remaining open risks have been substantially mitigated.
4. Members will recall that at the meeting of the Committee on 15 December 2014, it was agreed that a report on the Risk Register would be brought to each meeting of the Committee (Minute no. 15 refers). An updated version of the Risk Register has therefore been produced and is attached as Appendix 1. Members are asked to consider the risks set out in the Register.
5. Members should note that only two risks at this point remain open as the EfW Plant has now achieved Actual Takeover and both assessments of these risks are Green,
6. A copy of the Mercia Waste Loan Facility Drawdown Analysis is attached as Appendix 2.

Contact Points

County Council Contact Points

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Worcestershire Hub: 01905 765765

Specific Contact Points for this report

Sean Pearce – Chief Financial Officer

Tel: 01905 846268

Email: spearce@worcestershire.gov.uk

Supporting Information

- Appendix 1.1 Risk Register Open Risks
- Appendix 1.2 Risk Register Closed Risks
- Appendix 2 Mercia Waste Loan Facility Drawdown Analysis

Background Papers

In the opinion of the proper officer (in this case the Chief Financial Officer) the following are the background papers relating to the subject matter of this report:

Agenda papers and Minutes of the meeting of the Waste Credit Governance Committee held on 15 December 2014.

Waste Credit Committee Risk Register - Open Risks

March 2017 - Corporate Scoring Terms

Risk Reference	Description of risk	Gross Impact	Gross Likelihood	Gross Risk Score	Risk control approach	Mitigating Actions	Residual Impact	Residual Likelihood	Residual Risk Score	Assigned to (Risk Owners)
a Page 21	Default of loan repayments by borrower to lenders due to SPV (Mercia) or HZI falling into administration.	Critical	Medium	15	Risk transferred	Due to the security package negotiated by the Councils a fall away analysis indicated that Mercia, its Shareholders and HZI would need to have entered administration at the same time to put at repayment at risk during the construction phase. The maximum exposure to the Councils has been calculated and included within the sufficiency assessment of the Council's reserves. All press articles are scanned regularly for indications of financial strength issues and followed up to ensure counterparty risk is not increased. An example is where ACS Construcción and Services S.A., through its subsidiary ACS Servicios y Concesiones S.L., executed the sale recently of its total interest in URBASER S.A. To Firion Investments S.L.U, a company controlled by a Chinese group. The Councils then obtained legal advice that reassured lenders that no action was required by any parties arising from this change in ownership, as there were no changes to the Shareholder (Urbaser Limited).	Substantial	Very Low	6	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default and Deloitte to monitor Mercia's actual quarterly cash flow tests and cover ratios that have to be maintained by Mercia.
f	Mercia loan principal and / or interest repayments are below the required values as per the rates agreed in the STFLA .	Substantial	Very Low	6	Risk treated	The Council's treasury team maintain a spreadsheet detailing drawdowns to date and expected future principal and interest payments. This is reconciled to Mercia's repayment spreadsheet and will be matched to principal and interest repayments received from Mercia during the post construction period.	Substantial	Almost Impossible	5	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.

Key

High 19 – 24	Unacceptable Risk: Immediate control/improvement required
Medium 8 – 18	Acceptable Risk: Close monitoring and cost effective control improvements sought.
Low 1 – 7	Acceptable Risk: Need periodic review, low cost control improvements sought if possible.

Scoring Matrix

Likelihood

Very High	9	19	21	24
High	8	12	20	23
Medium	4	11	15	22
Low	3	10	14	18
Very Low	2	6	13	17
Almost Impossible	1	5	7	16
	Negligible	Substantial	Critical	Extreme

Impact

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Waste Credit Committee Risk Register - Closed Risks
March 2017 - Corporate Scoring Terms

Risk Reference	Description of risk	Gross Impact	Gross Likelihood	Gross Risk Score	Risk control approach	Mitigating Actions	Residual Impact	Residual Likelihood	Residual Risk Score	Assigned to (Risk Owners)	Reason why risk is closed
b	Construction completion date of EFW is delayed and delays repayment of loan to lenders.	Substantial	Medium	11	Risk transferred	Under the contract terms agreed with Mercia, Mercia take all material risk on EFW construction delay and repayment of the loans commenced on planned takeover date 28th February 2017, as set out in the SLFLA and agreed final financial model. Repayments are not tied to the actual construction completion date of 2nd March 2017, rather the planned date. The Council as lender also had the right to call the loan into default if construction was not completed by a long stop date.	Substantial	Almost Impossible	5	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.	Takeover took place on 2nd March 2017.
c	PWLB borrowing rates increase more than estimated in the Councils' prudential borrowing model. Higher rates would reduce the surplus generated on the loan arrangements with Mercia.	Substantial	Low	10	Risk treated	The cost of purchasing a financial product to remove this risk (a swaption) from an investment bank was quoted at £20m. The Councils decided to manage the risk through forecasting the forward price for its debt draw downs over the construction period and hold in reserve monies to mitigate this risk where required. The rates accessible by the Councils were lower than the estimate as the low gilt rate environment.	Substantial	Almost Impossible	5	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.	Takeover took place on 2nd March 2017. All loan payments have been made to Merca Waste and the rates gained from PWLB were below those estimated in the prudential model.
d	Loan drawdowns are slower than set out in the STFLA. Delayed drawdowns would result in reduced interest payments to the Councils and potentially reduced surplus if PWLB loan rates increase between the expected draw date and actual.	Negligible	Medium	4	Risk treated	The Councils borrowed from PWLB at dates in line with drawdown requests from Mercia. Therefore although the Councils will receive reduced interest receipts, less interest will also be paid to PWLB. The Councils monitored market gilt rates actively and had the option to borrow from PWLB up to a year in advance of expected drawdown requests. Regular progress reports were reviewed to ensure the construction programme and the loan drawdowns are requested in line with the plan.	Negligible	Almost Impossible	1	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.	Takeover took place on 2nd March 2017. All loan payments have been made to Merca Waste.
e	Drawdown requests from Mercia are not actioned by the Councils or not actioned within the required contracted time period.	Substantial	Low	10	Risk treated	The Council's treasury teams were fully briefed on the actions required to fulfil drawdown requests, checks required and the contracted timeline by the Section 151 Officer and their teams. Drawdowns were all actioned inline with requirements. Since the last Committee, two further drawdowns have been provided and there is a separate analysis available for the Committee outlining planned vs actual drawdowns made.	Substantial	Almost Impossible	5	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.	Takeover took place on 2nd March 2017. All loan payments have been made to Merca Waste within the required contracted time period.
g	Default of loan repayments by borrower to lenders due to HZI termination of Interserve Construction Limited (ICL) delaying project completion to after long stop date.	Critical	Medium	15	Risk treated	Sponsors provided assurance that they believe HZI undertook the right processes to replace the final ICL work packages and that there was no financial risk to the Sponsors. Sponsors confirmed that their Due Diligence on HZI had not raised any concerns around the company's viability or going concern. The Council as lender had the right to call the loan into default if construction was completed by a long stop date, at which point the negotiated security package, set out in section 'a' above, would have taken effect.	Substantial	Almost Impossible	5	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.	The final ICL work packages were replaced and takeover took place on 2nd March 2017.

h	<p>HZI termination of ICL may weaken negotiated security package due to no single new supplier exceeding £10 million contract value, and therefore triggering EPC Contract Schedule 7 requirements for Collateral Warranty and professional indemnity insurance requirements. The risk is that the Council as lender does not receive the same security package as it had when ICL was in place.</p>	Substantial	High	12	Risk treated	<p>In terms of Collateral Warranty, the HZI Collateral Warranty remained in place. Due Diligence was undertaken by Sponsors and the Council as Lender (with the Financial Advisor) confirmed the financial strength of HZI in light of events. There was no issues arising from these reviews. Sponsors agreed to review on a case by case basis the requirement for additional security protections and advised the Council as to its rational for its decision. The Council as Lender had sign off rights and requests were made to the Councils prospectively for Schedule 7 services and retrospectively (based on Sponsor Assurance) for non-Schedule 7 services. Meetings were held for sign off and Council advisors were retained to provide advice. The Councils clearly articulated to Sponsors that there should not be any weakening on the Security Package in place with regard to the Civil Engineering Work. All ICL work packages were replaced and there was no financial impact on Sponsors and therefore no financial impact on the Council as</p>	Substantial	Almost Impossible	5	<p>The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.</p>	<p>The final ICL work packages were replaced and takeover took place on 2nd March 2017.</p>
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Key

<p>High 19 – 24</p>	<p>Unacceptable Risk: Immediate control/improvement required</p>
<p>Medium 8 – 18</p>	<p>Acceptable Risk: Close monitoring and cost effective control improvements sought.</p>
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Almost Impossible	1	5	7	16
	Negligible	Substantial	Critical	Extreme
	Impact			

LOAN DRAWDOWNS

Mercia Waste Loan Facility Drawdown Analysis

March 2017

Key

	Planned drawdown paid to Mercia
	Planned drawdown overdue

Planned Drawdown Date	Planned Facility A Loan Drawdown (£) £	Planned Drawdown Date	Planned Facility B Loan Drawdown (£) £	Planned Total £	Actual Drawdowns £	Actual WCC share £	Actual Drawdown Dates
22-May-14	3,437,681	22-Apr-14	12,418,893	15,856,574	15,858,574	12,020,799	Drawdown 21/05/2014
31-May-14	1,138,388	31-May-14	4,112,516	5,250,904	5,250,904	3,980,185	Drawdown 05/06/2014
30-Jun-14	-	30-Jun-14	-				
31-Jul-14	-	31-Jul-14	-				
31-Aug-14	471,567	31-Aug-14	1,703,572	2,175,139			
30-Sep-14	284,368	30-Sep-14	1,027,302	1,311,670			
31-Oct-14	-	31-Oct-14	-				
30-Nov-14	956,758	30-Nov-14	3,456,362	4,413,120	7,899,929	5,988,146	Drawdown 11/02/2015
31-Dec-14	1,462,041	31-Dec-14	5,281,740	6,743,781			
31-Jan-15	425,251	31-Jan-15	1,536,253	1,961,504			
28-Feb-15	488,132	28-Feb-15	1,763,415	2,251,547	10,956,832	8,305,279	Drawdown 17/06/2015
31-Mar-15	922,698	31-Mar-15	3,333,319	4,256,017			
30-Apr-15	2,366,620	30-Apr-15	8,549,600	10,916,220	15,172,237	11,500,556	Drawdown 23/07/2015
31-May-15	2,400,673	31-May-15	8,672,622	11,073,295	11,073,295	8,393,558	Drawdown 21/10/2015
30-Jun-15	1,029,449	30-Jun-15	3,718,966	4,748,415			
31-Jul-15	1,315,749	31-Jul-15	4,753,246	6,068,995	10,817,410	8,199,597	Drawdown 25/11/2015
31-Aug-15	908,118	31-Aug-15	3,280,647	4,188,765			
30-Sep-15	1,209,552	30-Sep-15	4,369,603	5,579,155	9,767,920	7,404,083	Drawdown 01/02/2016
31-Oct-15	1,511,878	31-Oct-15	5,461,779	6,973,657			
30-Nov-15	1,550,833	30-Nov-15	5,602,507	7,153,340	14,126,997	10,708,264	Drawdown 25/02/2016
31-Dec-15	1,466,965	31-Dec-15	5,299,526	6,766,491			
31-Jan-16	567,125	31-Jan-16	2,048,785	2,615,910			
29-Feb-16	1,094,791	29-Feb-16	3,955,019	5,049,810	14,432,211	10,939,616	Drawdown 27/04/2016
31-Mar-16	1,021,353	31-Mar-16	3,689,717	4,711,070			
30-Apr-16	1,475,647	30-Apr-16	5,330,890	6,806,537	11,517,607	8,730,346	Drawdown 01/06/2016
31-May-16	1,197,470	31-May-16	4,325,954	5,523,424			
30-Jun-16	147,926	30-Jun-16	534,393	682,319			
31-Jul-16	139,033	31-Jul-16	502,267	641,300			
31-Aug-16	536,246	31-Aug-16	1,937,231	2,473,477	9,320,520	7,064,954	Drawdown 23/12/2016
30-Sep-16	586,749	30-Sep-16	2,119,676	2,706,425			
31-Oct-16	347,437	31-Oct-16	1,255,142	1,602,579			
30-Nov-16	166,670	30-Nov-16	602,109	768,779			
31-Dec-16	456,064	31-Dec-16	1,647,566	2,103,630			
31-Jan-17	1,002,431	31-Jan-17	3,621,359	4,623,790	11,805,203	8,948,344	Drawdown 03/02/2017
28-Feb-17	3,359,702	28-Feb-17	12,137,189	15,496,891	15,496,891	11,746,643	Drawdown 28/02/2017
Total	35,445,365	Total	128,049,165	163,494,530	163,496,530	123,930,370	

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WASTE CREDIT GOVERNANCE COMMITTEE

24 March 2017

WAIVERS/CONSENTS

Recommendation

- 1. The Chief Financial Officer recommends that the waivers/consents granted during the period under review be noted.**

Introduction

2. As set out in its Terms of Reference, the Committee will need to monitor and administer the loan to the waste project in line with best banking practice, including the terms of any waivers or amendments which might be required or are desirable.
3. The Chief Financial Officer has delegated authority for the day to day management of the waste management contract including waivers and consents that are not material to the STLFA to the Section 151 Officers.

Waivers/Consents requests

4. For the period under review the following waivers/consents were requested by the Sponsors and approved by the Councils:
 - In March 2017 the Councils provided a waiver/consent under clause 18.4(b)(K) of the Senior Term Loan Facility Agreement in relation to the issuance of a take-over certificate without the prior written consent of the Lenders. The waiver/consent was provided by the Councils on the basis of appropriate expert advice
 - In March 2017 the Councils provided a waiver/consent under part c of schedule 6 of the Senior Term Loan Facility Agreement in relation to a time deductible per occurrence contained within the Business Interruption Insurance Policy procured by the Borrower. The waiver/consent was provided by the Councils on the basis of appropriate expert advice.

Contact Points

County Council Contact Points

County Council: 01905 763763

Worcestershire Hub: 01905 765765

Specific Contact Points for this report

Sean Pearce – Chief Financial Officer

Tel: 01905 846268

Email: spearce@worcestershire.gov.uk

Background Papers

In the opinion of the proper officer (in this case the Chief Financial Officer) there are no background papers relating to the subject matter of this report.