

Agenda

Waste Credit Governance Committee

Tuesday, 12 April 2016, 2.00 pm
County Hall, Worcester

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(Kurdish) کوردی سۆزانی، نەگەر ناتوانی تێبەگەیی لە ناوێکی نەم بێلگەییە و دەستت بە هیچ کەس ناکەیت کە وەبێگێڕێتووه بۆت، تەکنیە تەلەفۆن بکە بۆ ژمارەی 01905 765765 و داوای پێنوێنی بکە.

ਪੰਜਾਬੀ। ਜੇ ਤੁਸੀਂ ਇਸ ਦਸਤਾਵੇਜ਼ ਦਾ ਮਸ਼ਹੂਨ 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

Tuesday, 12 April 2016, 2.00 pm, County Hall, Worcester

Membership: Mr W P Gretton (Chairman), Mr L C R Mallett (Vice Chairman),
Mr R C Adams, Mrs S Askin, Mr R W Banks, Mr M H Broomfield,
Mr P Denham and Mr P A Tuthill

Agenda

Item No	Subject	Page No
1	Named Substitutes	
2	Apologies/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 11 April 2016). 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 14 December 2015 (previously circulated)	
5	Actual construction period cash flow test	1 - 16
6	Progress summary from technical advisors	17 - 22
7	Risk register	23 - 30
8	Waivers/Consents	31 - 32

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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: Friday, 1 April 2016

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WASTE CREDIT GOVERNANCE COMMITTEE

12 APRIL 2016

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;
and**
 - 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 2015 of [£3,939k]. The result shows that in the period from 1 May 2014 to 31 December 2015, the operations have produced £3,939k 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 1 – Actual Construction Period Cash Flow Test
- Appendix 2 – Timetable for the production and review of the 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

Page 3

For the period:
1 September 2015 to 31 December 2015



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 a Waste to Energy (“WtE”) 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 VfM, the Councils used their prudential borrowing powers to debt fund Mercia’s WtE 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.

* Subject to the decision of the Councils regarding the January 2016 Unitary Payment (see page 5 and Appendix 1).

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;
- 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 to 31 December 2015.

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 2015 of £3,939k*.

This shows that from 1 May 2014 to 31 December 2015, the operations have produced £3,939k* more than was forecast for this period in the Base Case Financial Model.

Based on the above, the ACPCFT for the 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
Base case financial model						
<i>b/f cash attributable to Ops</i>	4,254	4,793	7,051	9,123	11,246	13,203
Gross revenue	18,603	10,448	10,847	11,813	12,374	10,627
Operating costs	(14,893)	(8,111)	(8,320)	(8,961)	(9,253)	(8,590)
Changes in working capital	(1,212)	320	(18)	(252)	(37)	451
Cell preparation assets	(612)	0	0	0	(632)	0
Corporation tax	(1,346)	(400)	(437)	(477)	(494)	(303)
Total change	539	2,258	2,072	2,122	1,957	2,185
Actuals						
<i>b/f cash attributable to Ops</i>	4,637	6,480	11,674	10,423	12,333	14,218
Gross revenue	19,688	13,341	10,578	11,929	12,091	10,523
Operating costs	(15,557)	(8,588)	(8,509)	(9,372)	(9,682)	(8,916)
Changes in working capital	(1,392)	1,363	(3,018)	(171)	(131)	3,331
Cell preparation assets	(333)	(286)	0	0	(189)	0
Corporation tax	(563)	(636)	(302)	(476)	(204)	171
Total change	1,843	5,194	(1,252)	1,910	1,885	5,109
Variance	1,304	2,936	(3,324)	(212)	(72)	2,924
Excess cash flow a/c b/f	383	1,687	4,624	1,299	1,087	1,015
Excess cash flow a/c c/f	1,687	4,624	1,299	1,087	1,015	3,939*

Source: Mercia; Financial Model; Senior Term Loan Facility Agreement. * Subject to the decision of the Councils regarding the January 2016 Unitary Payment (see page 5 and Appendix 1).

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 period under review is an Excess Cash Flow amount of £3,939k*.
- This means that in the period from 1 May 2014 to 31 December 2015, the operations have produced £3,939k* more than was forecast for this period in the Base Case Financial Model.
- 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.
- We note that despite the Excess Cash Flow amount at £3,939k*, there have now been four consecutive periods of under-performance against the modelled forecast.
- From discussion with Mercia, the underperformance reflects tighter recyclable materials pricing in 2015 and reduced revenues and increased costs whilst new glassbreakers were being installed.
- Installation of the glassbreakers was forecast for Q3 2014 but had been delayed until Q4 2015 due to extended lead times on supply.
- Since the installation of the glassbreakers, costs have reduced and additionally, recyclable materials pricing has seen marginal increases in the current year (2016). As a result of these factors, Mercia are projecting an increase in the Excess Cash Flow for the next quarter.
- This situation¹ should continue to be monitored closely.

¹ As well as other the financial covenants; * Subject to the decision of the Councils regarding the January 2016 Unitary Payment (see page 5 and Appendix 1).

Revenue down and operating costs up against modelled forecast

- We note that for the period under consideration, revenue actuals were 1% below the modelled forecast, but operating costs were 5% above the modelled forecast.
- Quarter 4 2015 saw a drop in recycling revenue as there was a shutdown period at the Materials Reclamation Facility whilst glassbreaking equipment was installed.
- During the installation period of 3 to 4 weeks there was no recycling sales output, but also increased third party costs due to the fact that Mercia had to pay for processing during installation.

Early Unitary Payment

- As with the prior year, the January Unitary Charge was paid early to Mercia (£3,672k).
- Again, Mercia contend that *"this is not "extra" cash, but normal operating cash received a few days early. The Council payments usually arrive in the first few days of the month, but in December the payment arrived on 31 December. If the definitions are to be followed strictly, we would be denied access to this cash until such time as the next Cash Flow Test is due"*.
- This treatment would reduce the variance shown for 1 October 2015 to December 2015 by £3,672k so that the cumulative Excess Cash Flow c/f to 31 December 2015, would be £267k rather than £3,939k. This treatment is in line with that proposed for the 31 December 2014 period.

Commentary (continued)

Early Unitary Payment (continued)

- Note that the full early payment was £4,115k, but £443k was relating to capital expenditure rather than operating and therefore was excluded as appropriate.
- This effect of this adjustment will be reversed in the next quarter. Deloitte will ensure that this is completed as appropriate.

ACPCFT trend

- We note that whilst the Excess Cash Flow amount is still positive (at £3,939k or £267k*), there have now been four consecutive periods of under-performance against the modelled forecast (i.e. an in period negative variance of actuals against the model).
- From discussion with Mercia, the key differences have been the drop in pricing for recyclable materials, and the reduced revenue and additional costs relating to the during the installation of the glassbreaking equipment.
- Installation of the glassbreakers was forecast for Q3 2014 but had been delayed until Q4 2015 due to extended lead times on supply.
- This also partly explains the positive performance in the early quarters of the test and subsequent underperformance since the revenue reduction during the 4 week installation period materialised in Q4 2015 rather than Q3 2014.

- It is understood that the installation has now been completed and the plant is now working as expected. We also understand that the anticipated drop in sub-contractor costs is materialising in Quarter 1 2016.
- Furthermore, Mercia contend that recyclable materials pricing has seen some marginal increases in the current year (2016), though Deloitte have not validated this.
- As a result of these factors, Mercia are projecting an increase in the Excess Cash Flow Account for the next quarter.
- We also understand that there are no similar delayed projects that could have a comparable impact on revenues and costs/
- As a result, Mercia believe that there is no cause for concern with regard to the ACPCFT trend over 2015.
- In any case, should the ACPCFT be failed in subsequent quarters, the process to resolve this has been extracted and included in Appendix 2.

* Subject to the decision of the Councils regarding the January 2016 Unitary Payment (see page 5 and Appendix 1).

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	Cumulative
Model							
Facility A	5,241	2,341	1,725	5,633	3,205	4,249	22,394
Facility B	18,898	8,426	6,190	20,288	11,490	15,241	80,535
Total	24,139	10,767	7,916	25,921	14,695	19,490	102,928
Actual							
Facility A	4,576		1,713	2,375	3,289	4,746	16,700
Facility B	16,532		6,187	8,581	11,883	17,145	60,328
Total	21,108	0	7,900	10,957	15,172	21,891	77,028
Difference	(3,031)	(10,767)	(16)	(14,965)	477	2,401	(25,901)

Facility A is the amortising loan. Capital repayment begins in the quarter ended 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 ended 31 December 2023.

From discussion with Mercia management, the lack of draw down in October 2014 to December 2014 period reflects both a delay in the WtE build (meaning less cash was required for the WtE build) and the lower than expected capital expenditure in non-WtE build (meaning that more cash can be used on the WtE build).

In the quarter to 30 June 2015, the draw down was also significantly below the modelled expectation. From discussion with Mercia management, the lower than forecast draw downs are due to the fact that, in general, there have been delays in the timing of some of the EPC milestone payments and the asset replacement programme has been a little behind due to the lead times for delivery / installation. These are delays in the timing of capital expenditure payments, and Mercia anticipate catching up with the model drawdowns later this year. This has partly been the case in Q3 and Q4 of 2015.

Source: Mercia; Financial Model

Appendix 1

Mercia's calculation (£000)

Cash Flow Test Calculation

	1 Oct 15 to 31 Dec 15 ACTUAL	1 Oct 15 to 10 Dec 15 MODEL
Profit Before Depreciation and Tax	1,607	2,037
Working Capital Movement (Operating)	3,331	451
Cell Preparation Assets	-	-
Corporation Tax (Cash)	171	-303
Operating Cash Flow	5,109	2,185

Excess Cash Flow

	1 Oct to 31 Dec 2015		
	Actual	Model	Var
Operating Cash Opening Balance	14,218	13,203	1,015
Operating Cash Flow (as above)	5,109	2,185	2,924
Operating Cash Closing Balance	19,327	15,388	3,940

Early Payment received from Council (31.12.15)	4,115
Element of payment that relates to Capex, not Operating cash	443
Element of payment that relates to Operating cash	3,672

Excess Cash Flow, after adjusting for Early Receipt **267**

Source: Mercia; Mercia also provided the workings behind this calculation so that the calculation could be reconciled to the company's trial balance and so it could be presented in a manner mapping to the description in the Senior Term Loan Facilities Agreement (see page 4).

Mercia's cash flow notice

<i>Excess Cash – Opening Balance (Sep 2015)</i>	1,015
<i>Gross Revenue</i>	-115
<i>Operating Costs</i>	-710
<i>Changes in Working Capital</i>	-397
<i>Corporation Tax</i>	+474
<i>Total</i>	-748
<i>Excess Cash – Closing Balance (Dec 2015)</i>	267

Appendix 2

Extracts from Senior Term Loan Facility Agreement

"Actual Construction Period Cashflow Test" means the quarterly test to be carried out on each Actual Construction Period Cashflow Testing Date, in relation to the preceding quarter period to determine whether:

- (a) actual Operating Cash generated during that period plus the brought forward cash balance attributable to operations is equal to, or exceeds;
- (b) 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 Cashflow Testing Date" means each Quarter Date following Financial Close, up to and including Completion;

"Actual Construction Period Cashflow Shortfall" has the meaning given to it in clause 15.9 (Actual Construction Period Cashflow Test);

"Actual Construction Period Cashflow Remedy Amount" means the minimum amount necessary following a failure by the Borrower of the Actual Construction Period Cashflow Test, to pass such test;

"Actual Construction Period Excess Cashflow 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 Cashflow Test;

"Base Case 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; plus
- (b) interest earned on all cash accounts (other than the Distribution Account); plus
- (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 that Financial Year, as reflected in the operating cashflow calculation in the Approved Financial Model;

"Working Capital" means Current Assets minus Current Liabilities.

Source: Senior Term Loan Facility Agreement

"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 cost 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; and
- (e) development costs,

and in all cases, the equivalent lines thereafter in each Approved Budget and each Approved Financial Model;

- (b) 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 Cashflow Test

- (a) On each Actual Construction Period Cashflow Testing Date, the Borrower will provide evidence satisfactory to the Lenders (acting reasonably) that the Actual Construction Period Cashflow Test has been satisfied.
- (b) Where there is a failure by the Borrower to satisfy the Actual Construction Period Cashflow Test on any Actual Construction Period Cashflow Testing Date (an **"Actual Construction Period Cashflow 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 Cashflow 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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Quarter End Date	MWM to send test and back up	Deloitte questions on test	Deloitte report ready	Report to Credit Committee	Credit Committee Meeting
	<i>Quarter End + 6 weeks</i>	<i>Quarter End + 7 weeks</i>	<i>Quarter End + 8 weeks</i>	<i>CC Meeting – 2 weeks</i>	<i>CC Meeting</i>
31/03/2015	By 13/05/2016	By 20/05/2016	By 27/05/2016	By 24/06/2016	08/07/2016
30/06/2016	By 11/08/2016	By 18/08/2016	By 25/08/2016	By 15/09/2016	29/09/2016
30/09/2016	By 11/11/2016	By 18/11/2016	By 25/11/2016	By 30/11/2016	14/12/2016
31/12/2016	By 10/02/2017	By 17/02/2017	By 24/02/2017	TBC	TBC

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WASTE CREDIT GOVERNANCE COMMITTEE

12 APRIL 2016

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; and**
 - 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 31 January 2016 for consideration by the Committee and this is attached as an Appendix.

Contact Points

County Council Contact Points

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Worcestershire Hub: 01905 765765

Email: worcestershirehub@worcestershire.gov.uk

Specific Contact Points for this report

Sean Pearce – Chief Financial Officer

Tel: 01905 766268

Email: spearce@worcestershire.gov.uk

Supporting Information

- Appendix – Summary reports from Fichtner Consulting Engineers – up to 31 January 2016

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.

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MEMORANDUM

To:	Mark Forrester	Organisation:	Worcestershire County Council
cc:	Simon Lewis	Organisation:	Worcestershire County Council
From:	Kerry Booth	Our Ref:	S1291-2300-0005KSB
Date:	9 th March 2016	No. of Pages:	3
Subject:	Mercia LTA Construction Progress Summary – March 2016		

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 2016).

2 PROJECT PROGRESS

The current programme shows a target Take Over date of 28th February 2017, which is in line with the contractual Take Over date. Current progress suggests this remains achievable. This is an improvement compared to the progress at the time of our previous summary memo, when a delay of one month compared to the contractual Take Over date was predicted.

Construction of the bunker base slab was completed in January 2016, in line with the programme date. Pouring of the tipping hall foundations, installation of steelwork to support the tipping hall floor, and construction of the bunker lining wall has commenced. Despite some delays due to high winds, the second waste crane and final bunker roof module have been lifted into place. Following completion of these lifts, HZI confirmed that the tower crane would be demobilised. This was expected in February 2016, but we have not confirmed this activity has been completed.

Painting and fire boarding of the bunker west core rooms has progressed well in January, although works elsewhere on the admin block have been slow.

There has been a slight delay to commencement of the main building cladding on north side to avoid overhead working and disruption to the final structural steel works. This has required resequencing of the road construction. HZI maintain that both the cladding installation and road construction works will still be completed in line with the programme dates.

Installation of water steam cycle (WSC) pipework has progressed well and is close to completion in many areas. Installation of cable tray for the 11kV cables to the e-houses is now complete and cable pulling was due to commence in February 2016.

There have been issues with agreement of the wayleave between Western Power Distribution (WPD) and the trading estate which have caused a delay to pulling of the 66kV cable to site. As a result, it has been agreed with HZI that the contractual date for provision of an energised grid connection will be revised to 15th April 2016.

3 KEY PROJECT RISKS AND OBSERVATIONS

Afcon were appointed as the building services contractor in December 2015. Detailed drawings by Royal Haskoning have been reviewed and comments returned to HZI. A building services design review meeting was held on 2nd February 2016 at which all open comments were discussed. A follow up meeting was planned for late February 2016, to try and resolve the key outstanding points. Details of that meeting have not yet been provided to the LTA for review. Due to the tight timescales involved, prompt resolution of issues and timely installation works are key risks which the Owner's Engineer is closely monitoring.

There has been good progress in regard to the bunker and tipping hall civil works this month. With the exception of road construction at the -8m level, it is considered that civil works construction now represents a much lower risk to the completion date.

Health and safety on site is also currently considered a key risk, and is discussed further below.

4 FINANCIAL AND COMMERCIAL

Payments have now been made for twenty four milestone events. The cumulative amount which has been certified to date is £79,382,899.55. The LTA has issued eight payment certificates to allow drawdown on the senior loan.

To date thirty four Variation Orders have been issued. To date the net reduction to the contract price is £38,192, which covers all Variation Orders. There has been no extension of time for any Variation Orders issued to date.

5 HEALTH AND SAFETY

In November and December of 2015, there was a steady decline in health and safety standards on site. This was evident from the poor rigging practices and housekeeping observed on site. However, there was some improvement in January 2016, although further work is needed to regain the high standards attained earlier in the project.

Although HZI consider that the standard of health and safety on site is good when compared with other construction sites, they acknowledge that there is further room for improvement. As such, they have outlined a number of measures to be implemented though the coming months.

The Owner's Engineer will continue to monitor the situation and put pressure on HZI to further improve the situation through the weekly site meetings, and weekly health and safety audits.

Key performance indicators for January 2016 show that two injuries were reported, one of which required an ambulance to attend site. There was also a serious near miss where petrol leaked from a Stihl saw onto an operatives clothing and caught fire. The fire was quickly put out using a nearby extinguisher and the operative was unhurt, although shaken.

52 Site Safety Observation Reports (SSORs) were raised in January, with the most common categories of report concerning safe access and egress, work at height, and the use of personal protective equipment. Five yellow cards and one red card were issued in January. One yellow card was issued in relation to personnel protective equipment (PPE) while the others concerned issues associated with working at height. The red card related to smoking on site.

6 PLANNED ACTIVITIES NEXT PERIOD

The following activities are planned from February 2016:

- Detailed engineering of remaining packages (including update of the HAZOP file, pedestrian footbridge, traffic impact study, external services layout, gatehouse steel structure, etc);
- Factory inspections for the WSC piping and maintenance hoists, which will conclude the manufacturing works of the main packages and the factory inspection programme;
- Continued work on civil packages including construction of access roads, fire hydrant mains, drainage, tipping hall, boiler hall, admin building, and completion of snagging and outstanding works on the turbine hall; and
- Continued work on process packages including boiler hall steelwork installation, closing of snags in the boiler assembly, continued installation of the FGT system, continued installation of turbine hall pipework and closing out of turbine hall snags.

Yours sincerely
FICHTNER Consulting Engineers Limited



Kerry Booth
Consultant



Phin Eddy
Commercial Director

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WASTE CREDIT GOVERNANCE COMMITTEE

12 APRIL 2016

RISK REGISTER

Recommendation

- 1. The Chief Financial Officer recommends that:**
 - a) The unmitigated and mitigated risks set out in the Risk Register be considered; and**
 - 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 has been established which sets out the unmitigated and mitigated risks associated with the loan arrangements.
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. 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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Email: worcestershirehub@worcestershire.gov.uk

Specific Contact Points for this report

Sean Pearce – Chief Financial Officer

Tel: 01905 766268

Email: spearce@worcestershire.gov.uk

Supporting Information

- Appendix 1 – Risk Register
- 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

April 2016 - 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)	
Page 25	a	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 enter 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.	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.
	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 loan will commence around February 2017, as set out in the SLFLA and agreed final financial model. Repayments are not tied to the actual construction completion date, rather the planned date. The Council as lender has the right to call the loan into default if construction is not completed by a long stop date. The Lender's Technical Advisor has confirmed that the expected Takeover Date is now the Planned Take Over Date, 28th February 2017.	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.
	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. Currently the rates accessible by the Councils are lower than this estimate as the continued low gilt rate environment pervades.	Substantial	Very Low	6	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.
	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 plan to borrow from PWLB at dates in line with drawdown requests from Mercia. Therefore although the Councils would receive reduced interest receipts, less interest would also be paid to PWLB. The Councils are monitoring market gilt rates actively and have the option to borrow from PWLB up to a year in advance of expected drawdown requests. Regular progress reports are being reviewed to ensure the construction programme and the loan drawdowns are requested in line with the plan	Negligible	Very Low	2	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.

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 have been 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 to date have been 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 to date.	Substantial	Very Low	6	The risk owners are the Section 151 Officers supported by Treasury and Financing Teams.
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.
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 have provided assurance that they believe HZI have undertaken the right processes to replace the final ICL work packages and that there is no financial risk to the Sponsors from the work underway. 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 has the right to call the loan into default if construction is not completed by a long stop date, at which point the negotiated security package, set out in section 'a' above, would take effect.	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.
Page 26	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.	Substantial	High	12	Risk treated	In terms of Collateral Warranty, the HZI Collateral Warranty is in place and remains in place. Due Diligence has been undertaken by Sponsors and the Council as Lender(with the Financial Advisor) to confirm the financial strength of HZI in light of events. There are 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 has sign off rights and requests have been made to the Councils prospectively for Schedule 7 services and retrospectively (based on Sponsor Assurance) for non-Schedule 7 services. Planned meetings have been held for sign off and Council advisors have been retained to provide advice. The Councils have clearly articulated to Sponsors that there should not be any weakening on the Security Package in place with regard to the Civil Engineering Work. There is no financial impact on Sponsors from events to date and therefore no financial impact on the Council as Lenders.	Substantial	Low	10	The risk owners are the Section 151 Officers of each Council supported by Ashurst as advisors in case of contract default.

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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LOAN DRAWDOWNS

Mercia Waste Loan Facility Drawdown Analysis

April 2016

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			
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			
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			
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			
28-Feb-17	3,359,702	28-Feb-17	12,137,189	15,496,891			
Total	35,445,365	Total	128,049,165	163,494,530	100,924,098	76,500,466	

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WASTE CREDIT GOVERNANCE COMMITTEE

12 APRIL 2016

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 December 2015 the Councils provided a waiver/consent under clause 18.4(b)(ii)(G) of the Senior Term Loan Facility Agreement in relation to the appointment of Afcon for the building services contract following the HZI termination of Interserve
 - In March 2016 the Councils provided a consent permitting the surrender of a small part of the lease within the EnviRecover leasehold back to the Councils, to enable the Councils, as landlord, to underlet to Western Power Distribution, who are constructing an electricity sub-station on a small plot of land. There is no increase in risk to the Councils resulting from provision of this consent, as a full Indemnity Covenant, is included in the legal documentation, on the part of the Adjacent Leaseholder, Mercia Waste, to the Landlord, the Councils.

Contact Points

County Council Contact Points

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Specific Contact Points for this report

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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.