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Waste Credit Governance Committee
Monday, 15 December 2014, 10.00 am, County Hall, Worcester

		Minutes
Present:		Mr W P Gretton (Chairman), Mr L C R Mallett (Vice Chairman), Mr R C Adams, Mrs S Askin, Mr M L Bayliss, Mr M H Broomfield, Mr P Denham, Mr J W Parish and Mr P A Tuthill
Available papers		The Members had before them: A. The Agenda papers (previously circulated); and B. The Minutes of the meeting held on 20 October 2014 (previously circulated).
9	**Named Substitutes (Agenda item 1)**	None.
10	**Apologies/ Declarations of Interest (Agenda item 2)**	None.
11	**Public Participation (Agenda item 3)**	Mr Rob Wilden addressed the Committee. He asked a series of questions in connection with issues raised in the Minutes of the Committee meeting held on 20 October 2014. The full text of the representation is appended to these Minutes together with the response that was sent to him. Mr Sheridan Tranter addressed to the Committee. He raised concerns about plant viability and air quality monitoring. The full text of his speech is attached as an appendix to these Minutes together with the response that was sent to him. Mrs Eve Jones addressed the Committee. She asked a series of questions in connection with issues raised in the Minutes of the Committee meeting held on 20 October 2014. The full text of the representation is appended to these Minutes together with the response that was sent to her.
12	**Confirmation of**	**RESOLVED that the Minutes of the meeting held**

Minutes (Agenda item 4)

on 20 October 2014 be confirmed as a correct record and signed by the Chairman.

At the request of the Chairman, the Chief Financial Officer explained the Terms of Reference of the Committee.

In response to the Chief Financial Officer's explanation, the following principal points were raised:

- It was apparent that the Technical Advisors – Fichtner Consulting Engineers were providing advice to the Council and to Mercia Waste Management. Did this represent a conflict of interest and as a result represent a major risk to the project? The Chief Financial Officer responded that there was a contractual obligation for the two teams within Fichtner Consulting Engineers to act completely separate from each other. He was satisfied that the assurance that had been given by the Technical Advisors regarding the creation of a "chinese wall" within their organisation mitigated any possible risks
- Were the questions raised by the public participants in relation to the technical operations of the facility within the remit of this Committee? The Chief Financial Officer explained that some of the issues raised by the public participants were outside the remit of the Committee. Their points had been addressed in three ways. Firstly, through the Cabinet decision-making process in the Council's capacity of Waste Disposal Authority; secondly, through the strategic commissioning arrangements; and thirdly, through on-site consultation
- In response to a query, the Chief Financial Officer undertook to make copies of his responses to the questions raised by the public participants available to members of the Committee
- It was important to understand that the role of the Committee was to consider the contract going forward and not re-examine previous decisions about the operation of the plant which were outside its remit.

13 Progress update from financial advisors (Agenda item 5)

The Committee received a verbal update from a representative of Deloitte, the financial advisors to the Council.

The Chief Financial Officer introduced Tim Dean who was a Manager at Deloitte. He explained that Deloitte had been engaged by the Council to act as the financial advisors to the Council. They had been appointed after a competitive tendering process and had been successful on the basis of their outstanding knowledge and experience in supporting the activities of commercial banks. Its role was to check the quality of the cash-flow tests and provide financial advice should any issues arise during the project. The cost of the service provided by Deloitte was fully rechargeable to Mercia Waste Management.

Tim Dean, the representative from Deloitte, informed the Committee that in relation to the latest cash-flow test, information had been received from Mercia Waste Management and further questions of clarification had been raised with them. A conclusion would be reached as soon as Mercia Waste Management had satisfied these queries. A Professional Standards Review would then be undertaken and the outcome of which would be reported to the Council. Mercia Waste Management was content that it had satisfied the terms of the agreement.

He added that Deloitte was also responsible for monitoring the draw down arrangements to ensure that they were in accordance with the financial model. To date, he was satisfied that the draw down arrangements were broadly in line with the model. Deloitte was responsible for reviewing the financial implications of construction period reports and at this stage there was nothing of significance to report to the Committee.

In the ensuing debate, the following principal points were raised:

- Did the cash-flow tests relate to all activities of Mercia Waste Management or specifically to this contract? The Chief Financial Officer advised that the tests related solely to the financial model for the project and the operations on site during the construction period
- Did the financial analysis of the project take into account the profitability to the shareholders? The Chief Financial Officer stated that due diligence tests had been carried out in relation to shareholders but the key issue was the status of the joint vehicle arrangements
- The report indicated that there was an excess cash-flow amount of £72,000, had this been confirmed by the cash-flow test? Tim Dean commented that the process included a series of tests and professional judgements by Deloitte. He

would liaise with the Chief Financial Officer to ensure that any professional judgements were kept within the context of the contract

- When would Deloitte be issuing the latest financial certificate to the Council and how frequently would it report in the future? Tim Dean explained that a certificate would be issued as soon as he was satisfied that Mercia Waste Management had supplied all the necessary information and provided satisfactory answers to the questions raised. He anticipated that a certificate would be issued shortly. Future certificates would be issued on a quarterly basis
- How much of the loan had Mercia Waste Management drawn-down to date? The Chief Financial Officer stated that to date, Mercia Waste Management had drawn-down £20m of the total loan amount of £165m. This money had been necessary for the enabling work at the site. It was anticipated that Mercia Waste Management would need to draw down funds at a faster rate as work on-site progressed
- In response to a query about the clarifications requested from Mercia Waste Management by Deloitte, Tim Dean commented that they related to some small differences between the financial information provided by Mercia Waste Management and the requirements set out in the financial model
- What was the timescale for the production of the next financial certificate? Tim Dean advised that this certificate had taken some time to prepare as this was a new process. He anticipated that future certificates would be produced more quickly. The Chief Financial Officer concurred and added that he was satisfied that there was not an issue with the project at present
- In response to a query, the Chief Financial Officer confirmed that the slippage of the schedule of the work on site would not have an impact on the cash-flow arrangements at this stage.

RESOLVED that the verbal update by Deloitte – Financial Advisors be noted.

14 Progress summary from technical advisors

The Committee received a progress summary from the technical advisors for October 2014.

The Chief Financial Officer introduced the report. He commented that:

(Agenda item 6)

- The summary report had been redacted to protect the commercial confidentiality of contractors and sub-contractors operating at the site
- The plant was due to open in 2017. Mercia Waste Management would still be required to repay the loan even if the plant failed to open on time
- The contractors working on behalf of Mercia Waste Management were aiming to open the plant 3 months ahead of schedule which therefore allowed a degree of slippage in the timescale for completion of the works on site
- At present work on site was four weeks behind schedule. The operators had begun dualling activities on the site and it was anticipated that the work would be on schedule by the end of quarter 2. At the moment the work programme was not considered to be at risk. Any major issues related to the timescale of the planned works would be reported to this Committee.

In the ensuing debate, the following principal points were raised:

- In response to a query, the Chief Financial Officer confirmed that Fichtner were one of the seven partner organisations that had approved the planned programme
- Committee reports should be as open as possible therefore concern was expressed that the report had been redacted on the basis explained by the Chief Financial Officer. The Chief Financial Officer undertook to raise the matter of redaction of future reports with the Monitoring Officer.

RESOLVED that the summary report from Fichtner Consulting Engineers – Technical Advisors be noted.

15 Risk Register (Agenda item 7)

The Committee considered the unmitigated and mitigated risks of the EfW project as set out in the Risk Register.

The Chief Financial Officer introduced the report and indicated that there were six key risks associated with the project. None of the residual risk scores had been identified as being red following mitigation measures.

The Committee considered each risk separately and in the ensuing debate, the following principal points were raised:

a) Default of loan repayments by borrower to lenders due to SPV (Mercia) or HZI falling into administration.

- The Chief Financial Officer explained that the maximum exposure of this risk to the Council was £6m. For this risk to become an eventuality, all seven companies involved in the project would need to go out of business. To mitigate that risk, the Council maintained a reserve of £12m. The risk to the Council would relate to the need to procure someone to replace Mercia Waste Management. He would maintain a watching brief on behalf of the Council over the financial affairs of all the companies involved in the project
- Was the Chief Financial Officer satisfied with the assurances being provided for the £600m refinancing of HZI? The Chief Financial Officer had raised the matter with representatives of the company and received assurances that its balance sheet had been strengthened by cash moved into the company as a result of its reorganisation
- On what basis was it determined that the maximum exposure of this risk to the Council be limited to £6m? The Chief Financial Officer explained that a range of financial security packages had been introduced at each stage of the supply chain e.g. insurances, bonds. Should each of the security packages need to be activated, then the maximum risk exposure to the Council would be £6m
- If the maximum exposure to the Council of the risk was £6m, why had the Council set aside a reserve of £12m? The Chief Financial Officer advised that the amount had been agreed by Cabinet and Council as a prudent approach to handling the risk
- The Chief Financial Officer undertook to inform members of the full name of the Spanish company providing the Parent Company Guarantee.

b) Construction completion date of EFW is delayed and delays repayment of loan to lenders.

- The Chief Financial Officer explained that any delay in the construction of the plant and consequently the planned takeover of the plant by the County Council would not impact on the loan being repaid by Mercia Waste Management. Mercia Waste Management had taken out insurance policies to mitigate the risks
- In response to a query about the risks borne by Mercia Waste Management, the Chief Financial

Officer stated the liquidated damages were to pay back the loan in the first instance. The first money at risk would be Mercia Waste Management's return on the £30m and the 30m itself

- What was meant by the reference in the mitigated action to a "long stop date"? The Chief Financial Officer explained that this was the date that the Council could forcibly stop the contract with Mercia Waste Management which would be 18 months after the construction date. At that stage the Council would be permitted to re-negotiate the contract.

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.

- The Chief Financial Officer stated that the Council's borrowing rates were set by the PWLB. The risk would be Gilt interest rates rose more than estimated in the Councils' prudential borrowing model above the rate set by the PWLB and thereby increased the cost of borrowing. Consideration had been given to purchasing a financial product to protect the Council against such a risk. However the product cost £20m and it was decided that the Council should instead maintain its own reserve. In addition interest rates had remained low and at present, the Council was saving more money than originally calculated.

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.

- The Chief Financial Officer explained that due to the slow start to the build programme, only £20m of funds had been drawn-down by Mercia Waste Management which was less than expected at this stage. At present, this was being offset by the PWLB loan rates remaining lower than estimated in the Councils' prudential borrowing model and also although the Council would receive reduced interest receipts, less interest would also be paid to the PWLB. The Council had built in prudent planning for any issues of this nature that might arise.

e) Drawdown requests from Mercia are not actioned by the Councils or not actioned within the required contracted time period.

- The Chief Financial Officer indicated that the Council had 8 working days in which to action draw-down requests from Mercia Waste Management. The Council's Treasury Management team were aware of the actions to fulfil the requests and all requests to date had been handled within 5 working days
- Did the Council have to finance loans through the PWLB or could it use its internal reserves? The Chief Financial Officer advised that the Council could be flexible with its approach. The Council had the option to draw from its monthly balance of £60-90m should it wish to. It was also possible to draw funding from the PWLB at short notice however approval of transactions of this nature required his signature. It was considered that the risk associated with this approach was low as if he was absent, his deputy had authority to sign the document.

f) Mercia loan principal and / or interest repayments are below the required values as per the rates agreed in the STFLA .

- The Chief Financial Officer explained that the Council's Treasury Team maintained a record of the draw-downs and expected future principal and interest payments. This record was then reconciled with Mercia Waste Management's record. There was a low risk that these records would be misaligned.

RESOLVED that:

a) the unmitigated and mitigated risks set out in the Risk Register be noted; and

b) a report on the Risk Register be brought to each Committee meeting.

16 Waivers granted (Agenda item 8)

The Chief Financial Officer informed members of the Committee that there were no waivers/consents to report for the first quarter.

The Committee noted that no waivers or consents were granted by the Chief Financial Officer in the last quarter.

The meeting ended at 11.25am

Chairman ……………………………………………….

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Ms Eve Jones – Waste Credit Governance Committee 15 December 2014

The following answers have been provided to the questions raised by Ms Eve Jones at the Waste Credit Governance Committee on 15 December 2014 where relevant to the Terms of Reference of that Committee.

Question	Response
1. It is stated that a report on the risk register would be brought to a future meeting. Are Councillors content that there is such a delay in providing this? Will it be provided today?	The risk register was presented to the Waste Credit Governance Committee (the Committee) on 15 December 2014 as requested and as planned. The Waste Governance Credit Committee met for the first time on 20 October 2014 to agree its terms of reference. As part of this exercise the Committee determined that it should receive an updated risk register at all of its meetings.
2. Please explain the statement "Mercia may wish to vary the contract (by means of a waiver or consent). The Contract was only signed in May at great cost and after having 16 years to get it right and after some councillors have stated that it was the Contract that was the problem!.	The statement was simply to identify a mechanism available in the loan facility agreement that can only be used subject to Council approval. The only example of where a request has been made to date was to seek agreement for an extension of time for submitting the revised financial model to the custodian. The consideration and approval of any waivers and consents are a standing agenda item for each meeting.
3. What is the view of the Committee regarding Council as lender, in a default situation, taking on shares or assets in Mercia in lieu of repayment of the loan?	The Council has negotiated a market standard loan facility. The rights available to the Council as lender were clearly set out and debated in the January 2014 Full Council
4. It is stated that the Council would be in a position to offer spare capacity to 'other users'. Is the Committee aware that there is over capacity in the West Midlands and other established incinerators can offer capacity at much less cost?	The Committee's terms of reference relate to ensuring loan repayments are secured. The question relating to plant capacity was covered as part of the December 2013 Cabinet Report and Variation Business Case and is not relevant to this Committee.

Question	Response
5. On 31st December 2023 the plant would be handed over to the councils. Please explain the statement regarding the 'need to borrow £0.25 Billion on one business day' as stated by the Chief Financial Officer.	This has been fully explained within the January 2014 report to Full Council. A link to that report is provided below. http://public.worcestershire.gov.uk/web/home/DS/Documents/Committees,%20Panels%20and%20Reviews/Council/Agendas%20and%20Reports%202014/Thursday,%2016%20January%202014.pdf
6. The Chief Financial Officer advised that HC and WCC needed to work closely together, how is this being catered for? KPMG, advisors to HC advised in 2013 that they should seek further advice and currently Herefordshire Council do not have a Waste Credit Governance Committee!	Officers meet on the lending side and have co-procured advisors to support the Councils on the lending arrangements. All lending advisors report to respective Chief Financial Officers. Equivalent business relating to the loan facility is governed through the Audit Committee at the County of Herefordshire Council.
7. The money and WIG credits for the incinerator planned at Kidderminster has been spent. This is now a new arrangement extra to that and using public money. What explanation is there for this installation being inferior to that planned at Kidderminster yet costing so many times more?	The relationship between WIG credits and project funding was covered by the December 2013 Cabinet Report. The choice of technology etc. was also covered within this report. It should be noted that notwithstanding this, the choice of technology is not within the remit of this Committee.

Mr Rob Wilden – Waste Credit Governance Committee 15 December 2014

The following answers have been provided to the questions raised by Mr Rob Wilden at the Waste Credit Governance Committee on 15 December 2014 where relevant to the Terms of Reference of that Committee.

Question	Response
1. "It was likely in the future; Mercia would wish to vary the contract (by means of a waiver or consent)". Could the Committee please explain exactly what they are referring to? Why is it considered likely that Mercia would wish to vary the contract – on what grounds?	Mercia may request a waiver or consent in relation to the Senior Term Loan Facility Agreement. Granting of any such waiver or consent is subject to the approval of both lenders. The statement was simply to identify a mechanism available in the loan facility agreement that can only be used subject to Council approval. The only example of where a request has been made to date was to seek agreement for an extension of time for submitting the revised financial model to the custodian. The consideration and approval of any waivers and consents forms a standing agenda item for each meeting.
2. "There were various actions that the County Council as lender could take in a default situation to provide security for the loan for example, taking on shares or assets in Mercia in lieu of repayment". How would shares or assets in Mercia provide security given that the WCGC Risk Register, December 2014, states that a default on the loan could only take place if "SPV (Mercia) or HZI fell into administration". How would the County Council benefit from shares in a company which is in administration?	The Councils as lender have successfully negotiated a number of significant protections around the loan facility as would normally be found in a lending facility. The scenario described where the lenders would need to take on the shareholders' interests in Mercia would see the lenders taking on agreements with existing subcontractors and/or appointing new ones. It must be recognised though that based on advice from its advisors, this scenario is extremely unlikely to occur.

Question	Response
3. In the WCGC Risk Register, December 2014, it states that default on the loan scores high and "represents a clear and present risk to the project". Mitigation relies on "the sufficiency of the Council's reserves". A Report in the 'Worcester News' recently stated that WCC has debts of £240m. Would the Council 'debt to revenue' ratio be able to sustain a further debt of £165 million in the case of a default? The Council has relied on making changes to their Treasury Policy Strategies and to their Statement of Prudential Indicators to provide an 'open ended' source of money to support the incinerator, seemingly limited only by the value of all the Council's total assets. Is this of any concern to the WCGC?	Risk Register reference a) sets out how the risk of default is being mitigated. The risk, prior to any mitigating actions is rated at Red. The mitigating actions are set out in the risk register that have resulted in a significant reduction to the risk rating. The risk register is a standing item of the Committee at each of its meetings. The changes that were required to be made to the Council's Treasury Management Strategy were set out and approved in the January 2014 Full Council Report. A link is provided below to that report. http://public.worcestershire.gov.uk/web/home/DS/Documents/Committees,%20Panels%20and%20Reviews/Council/Agendas%20and%20Reports%202014/Thursday,%2016%20January%202014.pdf
4. "The Chief Financial Officer explained that the Committee needed to understand the risks associated with the contract'. Is the WCGC only concerned with the due diligence of financing of the incinerator up until 2023? The PWLB was chosen partly to avoid delays caused by the due diligence procedures used by private lenders. Please state whether the WCGC has carried out due diligence beyond 2023? Has there been any commercial diligence carried out on the scheme to ensure a financial benefit to the Council as stipulated in the Parameters over the 25 year life of the incinerator? Is the absence of a business case beyond 2023 been a concern?	The Waste Credit Governance Committee has been established to oversee the life of the loan facility with Mercia. The January 2014 report to Full Council contains all information relevant to the assessment of the Council as lender to Mercia. A link is provided below to that report. http://public.worcestershire.gov.uk/web/home/DS/Documents/Committees,%20Panels%20and%20Reviews/Council/Agendas%20and%20Reports%202014/Thursday,%2016%20January%202014.pdf The December 2013 report to Cabinet sets out the Business Case for the Energy from Waste Plant that covers the full forecast operational period of the Energy from Waste Plant, beyond 2023. This business case was developed with the support of legal, technical and financial advisors. A link is provided below to that report. http://public.worcestershire.gov.uk/web/home/DS/Documents/Committees,%20Panels%20and%20Reviews/Cabinet/Agendas%20and%20Reports%202013/Thursday,%2012%20December%202013.pdf

Question	Response
5. The Council will need to refinance the unamortised loan of £123m in 2023 on the basis of the residual value of the incinerator at that date. Please state how the 'residual value sum' was arrived at given that there are no other second-hand incinerators on the market? How will the Council obtain a loan if the value of the incinerator is not as much as they predict?	The January 2014 report to Full Council contains information relevant to the assessment of the Council as lender to Mercia. A link is provided below to that report. http://public.worcestershire.gov.uk/web/home/DS/Documents/Committees,%20Panels%20and%20Reviews/Council/Agendas%20and%20Reports%202014/Thursday,%2016%20January%202014.pdf The Council will have already provided full financing to Mercia during the construction period and have secured financing arrangements via the Public Works and Loans Board. 2023 will represent a circular flow of funds (termed refinancing) whereby the Council as procurer will be required to pay to Mercia the outstanding balance of financing (known as the bullet payment) to allow Mercia to pay to the Council as lender this amount. This will mirror what would have occurred within a traditional commercial bank financing arrangement to ensure Mercia are not provided with any additional benefit through the financing arrangements.
6. "There is a risk that when the facility is handed over to the Council [in 2023] it would not be worth the payment of £128m". The WCGC suggests as mitigation that the Council will be able to offer capacity to other users. As spare capacity arising in the incinerator can only be sold for around half the unitary charge per tonne cost; what measures could the WCGC take to mitigate the possibility of the Council being unable to pay the full unitary charges, or the need to compensate for the shortfall in revenue caused by the use of substitute waste?	This question does not fall within the remit of the Waste Credit Governance Committee. The book valuation of the Energy from Waste Plant does not have any impact on the flow of funds to support the debt refinancing.
7. If the Council increases its recycling level above the 46% contracted level, spare capacity will arise in the incinerator. What measures can the WCGC take to ensure that the Council honours its 'minimum tonnage guarantee' to provide sufficient waste to the incinerator of a particular calorific value? Could penalty clauses be put in place as they have been with Mercia to help deter such an occurrence?	This question does not fall within the remit of the Waste Credit Governance Committee.

Mr Sheridan Tranter – Waste Credit Governance Committee 15 December 2014

The following answers have been provided to the questions raised by Mr Sheridan Tranter at the Waste Credit Governance Committee on 15 December 2014 where relevant to the Terms of Reference of that Committee.

Question	**Response**
1) Plant viability. I posed a question for Adrian Hardman 18th September, full council meeting regards the incineration project being of a reduced stature to that at Kidderminster, It is a single line i.e. one moving grate one furnace. "you have half an incinerator compared to the one envisaged at Kidderminster" Cllr Hardman said I was wrong. Yet my concerns are now being proved otherwise. After going to a drop in session held at very short notice by Mercia Waste (Public notice just three days) Ian Barber & the chief engineer answered some of my questions, the answers have only raised more. Question to Mercia's chief engineer " I have notice the design is for a single line incinerator, what will happen during maintenance, I have spoken to several engineers, they all stated the same, the weakest links are the conveyor belts (moving grate, its old technology) and fuel type. If the furnace shuts down it would be a major shut down. The linings have to be changed it takes weeks or months, Mercia's engineer stated two weeks working 24/7 (noise is an issue it could increase the cost) this scale doesn't stand with the industry standard of 89% or 7,796 hours (per year) this was stated in the planning, in short 40 days per year shut down. The maths: Waste 200,000 tonnes per year divided by 365.25 days = 547.57 per day bunker size capacity is 5 days only = 2,738 tonnes max Close down possible 40 days = 21,903 tonnes	This question does not fall within the remit of the Waste Credit Governance Committee.

Question	Response
Anything over 20 days is dangerous due to the build up of methane. Where will the waste go? no answers were given by the engineer or Ian Barber. I had the same response from one of you officers in October 2013. Even with the engineers comment of 14 days that's 7665.98 tonnes 2.8 times the size of the bunker. Waste decomposes and can self combust, that's what happened at Lawrence's in Kidderminster. Yes you have an incinerator but you were not informed that it only covers part of the waste stream part of the time. A two line plant never really shuts down. But as we know the affordability envelope could not allow for it, Deloitte reasoning. Strange you could have afforded it in 1998 with other beneficial methods, that are no longer in the revised contract.	
2) Air Quality monitoring. It is the biggest concern locally. I helped with a survey of 800 homes in the Hartlebury area, more than twice the turn out for the Parish elections responded, 96% of those polled stated that they didn't want the incinerator. I should imagine they would want air quality monitoring now, before the plant is built. It's not just the household concerned, the farmers are too, since many supply the major retailers, most of the land in the area is grade 1 or 2 arable land. Are you aware that only 15% of Worcestershire is grade 1.	This question does not fall within the remit of the Waste Credit Governance Committee.

Question	Response
At the same drop in meeting Ian Barber back tracked from what we had been told us that Mercia would put monitoring in before the building was commissioned. He stated that WCC regulatory Services should do it. Ian stated other businesses would not be happy if Mercia put air quality monitoring in. This should be seen as a plus since it would highlight any other pollution by others on the estate. i.e. the brick works where the filters have failed, or the waste tips that we have as well. Ian Barber did however state that he wanted to be good neighbours. Monitoring costs just £15,000 per year in relation to the incinerator it's just one eleven thousandth (£165,000,000 divide by £15,000 = 11000 times) the cost of the project build per year. Ian barber also stated " WCC and Mercia are joined at the hip" his words, so between you, you should be able to give a positive reassurance for Air quality monitoring to the residents of Hartlebury and Elmley Lovett, so that the accumulative effects can be measured before the plant is used.	

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