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Waste Credit Governance Committee
Monday, 23 February 2015, County Hall, Worcester - 10.00 am

Minutes

Present:

Mr W P Gretton (Chairman), Mr L C R Mallett (Vice Chairman), Mr R C Adams, 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 15 December 2014 (previously circulated).

A copy of document A will be attached to the signed Minutes.

17 Named Substitutes (Agenda item 1)

None.

18 Apologies/ Declarations of Interest (Agenda item 2)

An apology was received from Mrs S Askins.

19 Public Participation (Agenda item 3)

Mrs Eve Jones addressed the Committee. She asked questions in relation to Agenda item 6 – progress report from technical advisors. The full text of the representation is appended to these Minutes together with the response that was sent to her.

Mr Rob Wilden addressed the Committee. He asked questions in relation to Agenda item 7 – Risk Register. The full text of the representation is appended to these Minutes together with the response that was sent to him.

Mr Sheridan Tranter addressed the Committee. He asked questions in relation to Agenda item 6 – progress report from technical advisors. The full text of the representation is appended to these Minutes together with the response that was sent to him.

Why had the public participants to been prevented from raising other questions/comments? The representative of the Head of Legal and Democratic Services commented that public participation comments must be on matters on the agenda of the meeting. Some of the comments and queries raised by Mrs Jones and Mr Wilden related to the business of previous meetings. The agenda item on the minutes was a procedural one limited to approving the minutes as a true record of the previous meeting. It did not open up any wider discussion of matters in the minutes, even for elected members. Therefore Mrs Jones and Mr Wilden were informed that those comments and queries did not meet the constitutional requirements and were out of order and could not be presented.

In response to comments made by the public participants, the Chairman commented that he was satisfied that members of the Committee understood their role and provided necessary challenge to the advice provided by officers.

20 Confirmation of Minutes (Agenda item 4)

RESOLVED that the Minutes of the meeting held on 15 December 2014 be confirmed as a correct record and signed by the Chairman.

21 Progress update from financial advisors (Agenda item 5)

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

The Chief Financial Officer introduced the item and made the following points:

- The cash-flow test was necessary to provide assurance to the Council that Mercia Waste Management (Mercia) were able to sustain sufficient cash to qualify as equity. Two tests had been submitted both of which had satisfied the Council's criteria by some distance. The first test showed an in excess cash-flow of £1.6m against a target of £4.7m and the second test an in excess cash-flow of £1.19 against a target of £7.05m. Deloitte had been asked to confirm those numbers
- The majority of the cash-flow tests had been completed and Deloitte were now proceeding with the Partner Review process. He would liaise with the Chairman and Vice-Chairman to demonstrate that the Chief Financial Officer had signed-off the cash-flow test, following the Partner Review

- As the project moved onto the construction phase, ratio tests would be undertaken, which were financial health indicators. However these tests would not be required to be undertaken for some time
- The Council would only be concerned if the cash-flow test failed which was not the case at this stage. He expected that following the partner review, Deloitte would be in a position to sign-off the cash-flow certificate.

Tim Dean on behalf of Deloitte addressed the Committee. He commented that:

- The cash-flow tests would be carried out through the construction period on a quarterly basis with reference to the model agreed as part of the financial close in May 2014. In December 2014, Deloitte agreed the methodology for the cash-flow testing with all parties. An updated test for the previous period May – September 2014 and a test for October – December had been completed
- Two or three clarification questions had been raised with Mercia. However as explained by the Chief Financial Officer, the initial opinion was that the tests were satisfactory. The clarifications sought from Mercia were not significant or complicated and should Mercia be unable to supply satisfactory responses to them, it would not be a major issue. He anticipated a response from Mercia imminently.

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

- It appeared to take a significant period of time to receive the outcome of these tests, was there any way that the process could be speeded up? Tim Dean commented that the initial test had taken some time to provide because it was necessary to find an agreement with Mercia over the methodology for the cash-flow tests. This had now been agreed and there should not be any difficulty in providing timely information for future quarterly reports
- Was the representative of Deloitte concerned about the variation in both the ceiling of the cash-flow and the excess levels results between the two tests? Tim Dean responded that he was not concerned at this stage that the variations indicated a trend. He argued that the timing of the

initial cash-flow tests had had an impact on the variations and he anticipated that there would be a natural variation in the figures as the project progressed. However he would wish to challenge and ask questions of Mercia if it was felt that the expected cash-flow figures were at variance with the agreed model over a sustained period of time. The Chief Financial Officer added that should the cash-flow test prove to be unsatisfactory, the Council could decide not issue any further loan requests and request Mercia to inject sufficient cash-flow from Shareholders to meet the test

- Had a timescale been established for the signing-off of cash-flow test reports which aligned with meetings of this Committee? The Chief Financial Officer stated that meetings of this Committee had been scheduled on a bi-monthly basis. However, the cash-flow reports and the technical reports were quarterly reports. It was therefore proposed that meetings of the Committee be held on a quarterly basis. A timescale was being established to ensure that these reports accorded with the Committee meeting dates. A schedule of timings and responsibilities had been agreed with Mercia for the future
- A verbal report was satisfactory for the purposes of this meeting however, the Committee needed to be assured that the cash-flow tests had been signed-off. Future items should therefore incorporate a written report. The Chief Financial Officer agreed to provide these at future meetings.

RESOLVED that:

a) **the verbal update report from Deloitte – Financial Advisors be noted;**

b) **the Chairman and Vice-Chairman be authorised in liaison with the Chief Financial Officer to sign-off the Cash-Flow test, following the Partner Review; and**

c) **future final Cash-Flow test update information be received on a quarterly basis in written form.**

22 Progress update from technical advisors

The Committee considered the report from the technical advisors for the period up to the end of January 2015.

The Chief Financial Officer introduced the report and commented that:

(Agenda item 6)

- The aim of this report was to give the Committee assurance that the risk was being appropriately managed, of the plant being handed over in line with the planned takeover date and to ensure that the loan repayments were being made on time
- Mercia was committed to repay the loan from February 2017 whether the facility was constructed or not. Judgements were made on the progress of the project against that fixed date. Fichtner acknowledged that there had been a degree of slippage as a result of the more complex and difficult work undertaken during the initial development work on site. However there was an expectation that these delays would be recovered through the remainder of the project and it was still anticipated that the project would be completed 2 months ahead of the target date as per the agreed plan period.

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

- A 4 week delay over a 7 month period caused by a single contractor seemed a significant delay. Were Fichtner satisfied that this delay would not impact on the ability to deliver the project going forward? The Chief Financial Officer advised that Fichtner had acknowledged that there had been a delay but had not flagged it as a significant risk which would put the planned takeover date at risk
- The report from the Fichtner indicated that the amendments to the planning consent had been accepted as non-material however it went on to state that there remained a significant risk to the project that the revised drawings had not yet been submitted or approved by the local planning authority. What did the variation consist of and what were the associated risks? The Chief Financial Officer stated that Mercia had worked closely with officers in the Business Environment and Community (BEC) Directorate on these issues. He would circulate details of the variation and associated costs to members of the Committee. He emphasised that Fichtner had not raised this matter as a significant risk
- The report from Fichtner had indicated that there had not been any further drawdowns to report and yet a drawdown of £7m had taken place on 11 February 2015. The Chief Financial Officer explained that the drawdown took place after the

date of the technical advisor's report and therefore was too late to meet the timetable for the production of the report by Fichtner. This might occur again in the future and if this were to be the case, the Chief Financial Officer would update the Committee to ensure it had the most up to date information

- Was there a summary project plan available to members that listed the key project details so that members could relate to what was happening on the site? The Chief Financial Officer commented that there was a project plan which was monitored on behalf of the Waste Disposal Authority by the Director of BEC in liaison with the Cabinet Member with Responsibility
- What long term risks were associated with the residual value of the plant, for example depreciation in value of the plant in the market place? The Chief Financial Officer commented that the report to Cabinet in December 2013 addressed this issue. The Committee would still have a role in overseeing the loan repayments until 2023 to exert due diligence on Mercia. The residual value of the asset did not impact on the obligation for Mercia to repay the outstanding bullet tranche of loan at 2023. The residual value of the plant was a key matter for the Authority as purchaser of the facility and was kept under review by officers supporting the Cabinet Member with Responsibility for Environment
- What was the reason for the delay of the drawdown for the 31 December? The Chief Financial Officer advised that the manner in which Mercia draw down would inevitably be different to the financial plan. This was kept under review and would be reported to the Committee as it had done at this meeting. The lag in draw-down did not cause a concern at this point but if compared with other information about the project – the one month delay from the early opening planned by the contractor was consistent with other information held on the project
- The drawdown analysis showed that between August and January only approximately £8m had been drawn down from a planned target of approximately £15m. Why was there such a significant differential from the forecast and was the project on target for its completion in February 2017? The Chief Financial Officer explained that this was not a significant amount in the context of the total loan facility of £165m. He would expect

Fichtner to inform him if it thought that the project was put at risk as a result of the drawdown position. The plant remained on schedule to open 2 months earlier that the planned takeover date. In addition, the reduction in the amount drawn down had positive budgetary implications for the Council

- In response to a query, the Chief Financial Officer explained that there was only one set of loans both of which were termed senior loans. For clarification purposes, future reports would refer to them as the loan facility
- What was the difference between an A tranche and a B tranche? The Chief Financial Officer stated that the A tranche was a loan that Mercia repaid over the life of the contract. The B tranche was bullet tranche loan which represented a single payment to the Council by Mercia in 2023.

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

23 Risk Register (Agenda item 7)

The Committee considered the mitigated and unmitigated risks set out in the Risk Register.

The Chief Financial Officer introduced the report and commented that:

- The previous reports on the Risk Register had provided risk ratings on the basis of a stand-alone project. However it had been decided to bring the project in line with the corporate RAG ratings for consistency and as a consequence there were some small changes since the last report. There had been minimal changes to the risk ratings but the colour associated with the rating had changed in certain areas. Therefore a number of ratings had moved from amber to green
- The corporate risk team had been consulted about the revised RAG ratings to ensure they were consistent with the corporate approach

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

- What would happen if the Council, as the lender, decided to call the loan into default? The Chief Financial Officer commented that the Council would enact its security package which had been negotiated with Mercia and was in line with banking best practice. The Council was in a stronger position with 2 shareholders to indemnify the project so that if one of the shareholders pulled out, the other was obliged to take-over the arrangements. Due diligence checks had been made on these organisations, had been reported within the January 2014 Council report and would continue throughout the life of the contract

- Who determined the size of the bonds and would they remain the same amount through the life of the contract? The Chief Financial Officer advised that the amount of the bonds had been agreed in consultation with the technical and financial advisors and would remain at the same amount throughout the construction period and the life of the contract, relevant to that particular bond. He would provide members with an explanation of how the construction bond values have been calculated
- In response to a query, the Chief Financial Officer undertook to provide members with details of the tonnage of waste sent to landfill and associated costs to the Council.

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.

24 Waivers granted (Agenda item 8)

The Chief Financial Officer confirmed that no waivers or consents had been granted over the last quarter. In future, written reports would be provided for this item. He confirmed that the issues associated with the waiver granted as reported to the October 2014 Committee meeting had subsequently been resolved.

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

The meeting ended at 11.10am

Chairman …………………………………………….

Ms Eve Jones – Waste Credit Governance Committee 23 February 2015

Written answers have been provided to those questions that have been raised by Ms Eve Jones at the Waste Credit Governance Committee on 23 February 2015 where relevant to the Terms of Reference of that Committee.

Question	Response
1. From the Fichtner report Mercia Waste management stated that they have not received any claim for additional payment from HZI. From that statement it would be assumed that they can do so. Is this one of the items that WCC have paid insurance against?	This is a matter for Mercia and its main contractor, HZI. The Council as Procurer has agreed to pay a price per tonne of waste disposed of by Mercia that was fixed, subject to indexation as part of the contract variation
2. Additionally who would bear the cost of all Variations which MWM state will be subject to the approval of Mercia's shareholders. Where are the taxpayer interests?	Mercia will bear the costs where agreed.

Mr Rob Wilden – Waste Credit Governance Committee 23 February 2015

Written answers have been provided to those questions that have been raised by Mr Rob Wilden at the Waste Credit Governance Committee on 23 February 2015 where relevant to the Terms of Reference of that Committee.

Question	Response
You have chosen to use the traffic light system to identify risk. You started with red areas thereby indicating serious concerns but I note from the papers for this meeting that all areas are now identified as amber or green, indicating that all is running relatively smoothly. I am concerned to ensure that this does not lead to complacency and that the risks are reviewed on a regular basis and questioned. You should not be reliant solely on the views of your Officer - you are accountable both pre and post the forthcoming elections and it is your responsibility and duty to challenge your Officer and such challenge is long overdue. I urge you to start making those challenges now.	Risks commenced as Red prior to actions taken by the Council. The majority then moved to Amber or Green at a project level based on mitigations put in place as set out in the risk register. It has been agreed now to make the RAG rating consistent with the Corporate rating and therefore the risk scores have not changed significantly. The Committee continues to monitor and challenge each risk at every meeting.

Mr Sheridan Tranter – Waste Credit Governance Committee 23 February 2015

Written answers have been provided to those questions that have been raised by Mr Sheridan Tranter at the Waste Credit Governance Committee on 23 February 2015.

Question	Response
1. Part 3 lacking in scope, we are talking here about a major civil engineering project which due to its size and area is being built on is proving troublesome at best. I remind you of what happened with Evesham's nice new bridge as an example. Projects of this nature have a poor record for ever being on time. top aspects of any projects: (time, funds, quality) any one of these altered will affect the others. What planning alterations? the general Public are not being informed of them, so are you?	The risk that is being overseen by the Committee is that the planned takeover date of the Plant is not met which may put the repayment of the loan at risk. The Committee are aware that although this would indicate a risk, Mercia is obligated to commence repayment of the debt even if there is a delay in Takeover Date past the Planned Takeover Date. The Committee takes comfort that whilst the risks have been transparently reported by the Lenders Technical Advisor, the Lenders Technical Advisor conclude that the Planned Takeover date is still forecast to be achieved. Any slippage is a risk borne by Mercia.
2. HZI has indicated that it has issued amended drawings only 25 working days ago, "a significant risk" the Local planning authority have not seen them. How are the Chinese Walls being maintained, who is monitoring this, what is the structure?	The County Council has undertaken appropriate Due Diligence, sought and obtained representations from Fitchner on the operation of Chinese Walls within the organisation. This includes for example separate teams, segregations in filings and reporting structures.
3. Pictures of the excavation where asked for but never given or even put on the website, which is what Mercia Waste said they would do, the question is why not?	This is a matter for Mercia, but we will pass on the request. We note that there is a time-lapse video on Mercia's website, http://www.severnwaste.com/recovery/site-progress/

Question	Response
4. Part 4 I note last paragraph: Mercia has instructed HZI for proposals regards installation, yet they state the following "Mercia noted that these proposed changes will be treated as cost Variations which will be subject to the approval of Mercia's shareholders "The question who is driving this, again this affects the quality, which then impinges on the other two main principles as stated above.	Whilst this relates to a technical report – the only reason for the Lenders' Technical Report is to confirm progress of the project and therefore flag any risks to the repayment of the loan – a response has been provided below. Any cost/quality risk is managed through the County Council's Waste Disposal Authority (Cabinet) relationship with Mercia as the purchaser of the service and not a point for this Committee. The County Council as procurer has procured the construction and operation of an Energy from Waste Plant as part of an overarching Waste Disposal contract that meets certain outcome criteria. Mercia has provided a price for this. In delivering their obligations, Mercia will work with its subcontractors to deliver their obligations. Should additional costs be incurred, these are negotiated and met by Mercia – a price for the outputs has already been agreed between the Council and Mercia. This is not a turn-key contract where the Council as procurer would then take risk on cost variations. Any material changes to how Mercia intend to deliver those output obligations are discussed by Mercia and the Councils' Waste Disposal team.