

AGENDA ITEM

REPORT TO CABINET

17 MARCH 2022

**REPORT OF CORPORATE
MANAGEMENT TEAM**

CABINET DECISION / KEY DECISION

Leader of the Council - Lead Cabinet Member – Councillor Bob Cook

TEES VALLEY WASTE PROJECT

SUMMARY

Cabinet have previously agreed to procure an Energy for Work Facility (ERF) in partnership with Tees Valley authorities, Durham County Council and Newcastle City Council and this has been outlined in reports to Cabinet in October 2019 and July 2020.

This report provides an update to Members regarding all aspects of the TV ERF project including planning, landowner, procurement process, the development of the Project Agreement and other project documents.

The report outlines the requirement and rationale for setting up the Local Authority Special Purpose Vehicle (LA SPV) between the partner authorities to manage the contract with the successful provider. It outlines how this will be governed as well as the commercial principles as to how costs / liabilities shall be shared between the seven Councils over the term of the Project

REASON FOR RECOMMENDATIONS/DECISIONS

The recommendations in this report are required to progress the arrangements for the Tees Valley ERF project.

RECOMMENDATIONS

1. A LA SPV is required to be established as a Limited Company incorporated and registered at Companies House. It will be the Contracting entity representing the seven Councils (the Shareholders) and will enter into the Project Agreement with the successful Contractor and the lease with STDC (Teesworks) for the site.

Cabinet are requested to approve the creation of the LA SPV.

2. The regulation and management of the LA SPV shall be governed by the Shareholders' Agreement (SHA). Each Council (Shareholder) will be required to formally enter into the Shareholders' Agreement approximately three months in advance of the Project Agreement being entered into with the successful Contractor (Financial Close).

Cabinet are requested to approve the Council entering into the Shareholders' Agreement and to Delegate Authority to the Director of Finance, Development &

Business Services in consultation with Cabinet Member and Director of HR, Legal & Communications.

3. The terms of the commercial arrangements between the seven Councils (the Shareholders) in relation to the LA SPV will be defined and governed by the Waste Supply and Support Agreement (WSSA). The WSSA is required to be formally entered into by the seven Councils (Shareholders) in parallel with the LA SPV awarding the Contract and entering into the Project Agreement with the successful Contractor.

Cabinet are requested to Delegate Authority to the Director of Finance, Development & Business Services in consultation with Cabinet Member and Director of HR, Legal & Communications to finalise and enter into the Waste Supply and Support Agreement with the LA SPV and to provide Delegated Authority from the Councils' perspective for the LA SPV to award the Contract and enter into the Project Agreement with the successful Contractor (Financial Close), and to enter into the 50-year lease with STDC (Teesworks) for the site.

4. Each Council will be required to enter into two 'Council Guarantees'. The first will be to provide resilience to the LA SPV and to provide comfort to the Contractor that the LA SPV is fundamentally robust to meet its obligations under the Project Agreement. The second is to underwrite the LA SPV's obligations (rent etc.) under the 50-year lease for the site.

Cabinet are requested to delegate authority to the Director of Finance, Development & Business Services in consultation with Cabinet Member and Director of HR, Legal & Communications to enter into the Council Guarantees.

5. A Business Plan for the LA SPV has been produced which details the 'structural' and operational costs of the Company.

Cabinet are requested to delegate authority to the Director of Finance, Development & Business Services in consultation with Cabinet Member and Director of HR, Legal & Communications to finalise and agree the Business Plan and provide sufficient resources to allow the LA SPV to reach Financial Close and then to monitor and manage the Contract on behalf of, and with, the Councils for the term.

DETAIL

BACKGROUND

1. Stockton Borough Council, Darlington Borough Council, Durham County Council, Hartlepool Borough Council, Middlesbrough Council, Newcastle City Council, Redcar and Cleveland Borough Council (the Authorities) have a statutory obligation to provide waste management services to their collective 1.5m residents.
2. The Councils currently operate residual waste disposal services as a group under a single contract with Suez and which includes Redcar and Cleveland Borough Council, Hartlepool Borough Council, Stockton Borough Council and Middlesbrough Borough Council. Darlington Borough Council is part of the group but currently has its own separate waste treatment and disposal contract. Durham County Council and Newcastle City Council currently have their own separate residual waste disposal contracts with SUEZ.
3. The Authorities have joined together to procure a contractor to design, build, operate and finance a new Energy Recovery Facility to be located in the Tees Valley (TVERF).
4. All existing waste treatment / disposal contracts are due to expire in 2025/26 and therefore

a new Residual Waste Treatment Contract must be procured in order to allow for the new facility to be constructed and fully commissioned in preparation for this. The Service Commencement Date for the new facility is the 1 April 2026.

5. Supported by Business Cases, the requirement is for a c.450,000 tonne per annum Energy Recovery Facility (ERF) with Combined Heat and Power (CHP) capability to treat the Councils' municipal solid waste, this being the residual waste that has not been (or cannot be) recycled. This combined tonnage unlocked economies of scale which were attractive to the Councils [and to the market] and encouraged them to commence this procurement together.
6. The ERF will be designed to have a minimum 40-year lifespan and the Contractor appointed following the conclusion of the procurement process will build, finance and operate the ERF. The initial contract term shall commence in 2022 (subject to entering into the Project Agreement with the successful bidder (Financial Close). The Contractor shall construct the facility in preparation for the Service Commencement Date on the 1 April 2026, at which point the Contractor is required to accept and manage all Contract Waste. The Contract shall terminate on the 31 March 2052, unless both parties agree the terms of a potential [eleven-year] extension that may run up until 2063.
7. The Contract will require the successful contractor to invest very significantly, likely to be several hundred million pounds, to construct the TV ERF. The procurement process is still underway, but it is expected that the total value of the Contract could be £2.1bn over the 29 years (plus 11 years) Contract. The facility will revert to the ownership of the Councils at the expiry of the Contract.
8. The TV ERF will be a source of renewable electricity (up to 49.9MW) equivalent to powering over 60,000 homes. It may be possible in the future to export the renewable heat which is generated by the facility, to be provided to local businesses and other local users of heat, should a future Business Case demonstrate this to be feasible (technically and economically) and provide overall Value for Money for such an investment.
9. To encourage competition, a 22-acre brownfield site, owned by South Tees Development Corporation, was selected within the Teesworks regeneration site and this is mandated for use by the successful Contractor.
10. The development will create a few hundred jobs during the construction phase and up to 50 permanent positions during the services phase. The residues from the process (including metals and bottom ash) will be recovered or recycled, thereby directly displacing the requirement within industry for additional virgin materials that would otherwise have been required. The facility will make a valuable contribution to the local circular economy.
11. Outline Planning Permission for the proposed development was issued by the Planning Authority in July 2020. Obtaining 'Full Planning Permission' for the development is a prerequisite for any of the three bidders to be appointed Preferred Bidder. A Local Authority Special Purpose Vehicle (a Limited Company) is required to be formed by the seven Councils as this will be the contracting entity with the successful Contractor.
12. Project governance continues to be provided by a Board made up of representatives of each of the seven Councils which normally meets on a monthly basis. The Board's terms of reference set out clear decision making and a voting structure and an escalation process in local authority special purpose vehicle.

Special Purpose Vehicle

13. A LA SPV is required for the management of the Project Agreement (in relation to the TV ERF project).
14. The LA SPV would be the party contracting directly with the Contractor and would be primarily liable to the Contractor for all payments under the Project Agreement.
15. Hartlepool Borough Council (as the Lead Authority) would enter into the option over the mandated Reference Site with STDC (prior to establishment of the LA SPV for contract signature) but the LA SPV would be the party entering the lease and therefore holding the leasehold interest in the Reference Site for the duration of the Project and thereafter, until expiry or reversion of the lease to STDC.
16. On expiry or termination of the Project Agreement, the Project assets (e.g. the ERF) would revert to the LA SPV (with the LA SPV becoming the owner of the ERF at that point).
17. The LA SPV would back off all its liabilities under the Project Agreement to the Councils through a Shareholders' Agreement (and/or IAA); and
18. The contractor will seek a right of direct recourse to the Councils to in effect stand behind the LA SPV's balance sheet (a guarantee or indemnity provided by the Councils for the benefit of the contractor).

Shareholders Agreement

19. The Shareholders' Agreement (SHA) sets out and defines the corporate governance and structure of the LA SPV itself. It will regulate the management of the Company and the relationship between the Councils as shareholders in the Company.
20. The Key Points from the SHA include the following:
 - The LA SPV will be a limited liability company incorporated in England and Wales.
 - Each Council shall hold a single share in the LA SPV and shall be entitled to one vote.
 - Each Council shall be permitted to appoint one Director to the LA SPV Board.
 - The Councils shall appoint a management team to carry out the day-to-day operations of LA SPV under the Project Agreement.
21. The Councils will be required to engage and provide the necessary resource so that matters to be decided by the LA SPV Board and/or the LA SPV Shareholder can be appropriately considered (where applicable within timescales required to enable LA SPV to satisfy its obligations under the Project Agreement).
22. Upon liquidation of the LA SPV and after discharge of all obligations associated with the winding down of the Project, any remaining assets of the LA SPV will be shared between the Councils in proportions equal to the overall tonnage of Contract Waste that each Council has supplied to the facility over its life.
23. The Councils will pay all legal, accountancy and other fees and expenses incurred by the LA SPV on a pro rata basis.

Waste Supply and Support Agreement

24. The Waste Supply and Support Agreement (WSSA) will deal with how the payment

obligations and financial liabilities of the LA SPV will be shared between the Councils.

25. The WSSA will be entered into on (or shortly before) the date of the Project Agreement and will continue until terminated by mutual agreement of the Councils. Upon the WSSA coming into effect, the First Inter-Authority Agreement (entered into on 24 July 2020) will terminate.
26. The payment obligations of the LA SPV will be supported by a guarantee entered into by all of the Councils on a joint and several basis.
27. The general principles for the allocation of liability between the Councils will be based on the proportion of tonnage delivered by each respective Council compared to the overall tonnages either on a Cumulative Contract Waste Tonnage to Date basis, or on the Council's share of the Guaranteed Minimum Tonnage (GMT).
28. The Contractor will be responsible for all Contract Waste from 1st April 2026.
29. Payments in respect of the Lease of the Site shall be allocated based on the actual tonnages supplied by each Council as a proportion of the total combined actual tonnage delivered by all seven Councils for the preceding Contract Year.
30. The WSSA is currently being drafted. Once it has been agreed by the Project Board, approval shall be sought from the Director of Finance, Development and Business Services in consultation with Cabinet Member and Director of HR, Legal and Communications.

LA SPV Business Plan

31. An Operating Cost Model for the LA SPV has been drafted which covers the period from incorporation of the LA SPV Limited Company until expiry.
32. The Operating Cost Model is being updated and refined. This will allow the Business Plan to be developed to ensure sufficient resources are provided by the Councils to allow the LA SPV to reach Financial Close and then to monitor and manage the Contract on behalf of, and with, the Councils for the term.

South Tees Development Corporation Lease

33. The total lease with STDC (now rebranded as Teesworks) will be a period of 50 years from financial close, with break clauses at Year 29 and each 5 year period thereafter.
34. The lease will allow for a period of c. four years to allow the construction of the ERF, followed by an initial period of 25 years (extendable to 40 years) covering the operational phase of the ERF.
35. The lease costs will apply from Service Commencement Date (1 April 2026) and will be £25,000 per acre per year (increased in line with indexation).
36. Service charges will be applied and shall take effect from the date of the signing of the lease.
37. Environmental Liability – the Authority is not responsible for existing (historical) ground contamination nor for any contamination which leaches into the site from surrounding land and watercourses during the term of the lease.

38. It has been agreed that biodiversity will be dealt with off-site by STDC (Teesworks) in return for a one-off, pro-rata contribution to STDC's costs of the off-site sterilised area (pro-rata to the area of the demised site as a proportion of the 2,500-acre whole), capped at £500k.
39. The obligation to remediate the site at the end of the lease (demolish the ERF and put the site back to its pre-construction state) sits with the Councils and will be at the Councils expense.

CONSULTATION AND ENGAGEMENT

40. The Tees Valley Authority Project Board receive regular monthly updates regarding the progress made on all aspects of the TV ERF Project.
41. All seven Authorities have been engaged with and consulted on the contents of the Shareholders' Agreement, Waste Supply and Support Agreement (Key Commercial Principles) and the LA SPV Operating Cost Model.

COMMUNITY IMPACT IMPLICATIONS

42. None

CORPORATE PARENTING IMPLICATIONS

43. None

FINANCIAL IMPLICATIONS

44. The financial implications of the LA SPV will be set out within the Business Plan. The treatment costs of the residual waste that shall be required to be paid to the Contractor and how these will be shared between the seven Councils will be defined within the Waste Supply and Support Agreement. The costs of the lease and the LA SPV will be incorporated into the costs of the gate fee charged to each Council.

LEGAL IMPLICATIONS

45. The procurement of the TV ERF and the formation of the LA SPV as the contracting entity representing the Councils' interests will have legal implications. The Shareholders' Agreement and Waste Supply and Support Agreement will bind the parties together in a robust and legally enforceable commercial arrangement.

RISK ASSESSMENT

46. The five Tees Valley Local Authorities along with Durham County Council and Newcastle City Council have agreed and implemented a robust risk management strategy to identify the key risk and ensure a consistent approach to both strategic and operation risk across the project.

The current waste disposal contract has already been extended and therefore a further extension of the contract without competition would be in breach of procurement rules and would subject the Authorities to the risk of challenge that could potentially delay the project. Additionally, the facility will be over 30 years old by 2025 raising significant risk of unpredictable maintenance costs and downtime

WARDS AFFECTED AND CONSULTATION WITH WARD/COUNCILLORS

47. Regular updates on the Project are provided to the Leader of the Council, Cabinet Member and Managing Director.

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