APPENDIX 3: Integrated Waste Handling Contract Evaluation and Background

Report title: Integrated Waste Handling Contract Service Delivery	
Report to: Cabinet	
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County Divisions affected: All Essex	

1. Overview

1.1 The report highlights the challenges associated with delivery of IWHC during an expected period of uncertainty for Essex and the broader waste industry. We are approaching this sourcing model decision leading into a period of flux in the areas below:

- **Local Government Reform** is upcoming although the date and content of the white paper is currently unknown
- The **Essex Waste Strategy** is under review and the **National Waste Strategy** impacts are unknown
- ECC will be called upon to deliver on statutory requirements for the **Environmental Bill** when it is enacted and to achieve **Strategic Objectives;** ambitions for waste management and sustainable approach to educate our population to reduce, reuse and recycle.
- The **MBT / Tovi Eco Park** which is currently in its commissioning phase is currently not accepting waste.

All of the above mean that are currently considerable unknowns on the horizon for this service. To require tenderers to build in potential and or unknown change into a contract of this scale adds **significant risk** to the provider and that comes at a cost.

1.2 ECC may require **considerable flexibility** on how the service is run. To align to any upcoming strategy ECC would need more control over the service than a fully outsourced model offers.

2 **Evaluation**:

2.1 To arrive at the recommended approach, officers from Finance, Organisation Development and People (ODP), Procurement, Service Operations, Technical and Service Strategy teams evaluated the viable options using qualitative and quantitative techniques.

2.2 **Qualitative Evaluation:** A combination of SWOT (success, weaknesses, opportunities and threats) analysis and options scoring was used to assess the relative qualitative merits of each option. The SWOT analysis and options scoring process was informed by a series of soft market testing events held during June, July and September 2020.

2.3 **Qualitative Assessment:** Officers then carried out a qualitative assessment of the 3 main options: Option A: Integrated outsourced, Option B: Disaggregated outsourced and Option C: Hybrid Sourcing Model.

2.3.1 The options were scored by individual officers to assess their likely performance in respect of the following criteria:

- Future financial savings
- Customer service
- Control / flexibility
- Continuous improvement
- In-house resource / deliverability
- Risk management
- Market appetite

2.3.2 Following scoring of the options against a set list of criteria by individual officers, consensus scoring was undertaken to arrive at a single set of consensus scores and supporting rationale evidence. A summary of the results of the consensus options scoring are set out in Table 1.

Table 1: Consensus Scoring Summary

Model	**Score (out of 70)**
Option A: Integrated	44
Option B: Disaggregated	41
Option C: Hybrid sourcing	49

2.3.3 A summary of the consensus results taken from the qualitative assessment is outlined below in Table 2. This concluded that Option C: the In-house Hybrid was the most advantageous from a quality perspective: scoring higher than all the other options in terms of control/flexibility, customer service and continuous improvement. It also scored well in respect of future financial savings and market appetite. However, Option C scored lower on risk transfer and in-house resource / deliverability. In order to mitigate against these particular risks and other risks identified during the development of the option, a risk register has been established and a copy can be found in Table 3 of this document.

Table 2: Consensus Summary

	Option A (Fully integrated outsourced)	
Evaluation Criteria	**Score**	**Rationale**
Future financial savings	7	Whilst the contract does allow for variations to reduce costs this only anticipates site closures as the way of achieving it. Additionally this variation process only enables ECC to achieve a percentage of the savings and not the whole saving achieved by the supplier. The current contract also doesn't encourage the supplier to come forward with savings ideas, therefore, it tends to be Authority led change.
Customer service	7	Contract contains a Performance Measurement Framework (PMF) that attenuates payments to the contractor where the service standards are not fully delivered. This is designed to incentivise the contractor to deliver high-quality services. However, the PMF does not cover all aspects of the user experience and therefore excellent customer service is not achieved. The contractor's attention tends to be directed towards aspects which impact contract profitability, rather than customer experience.
Control / flexibility	6	Contract contains a change mechanism that enables ECC to alter its service requirements within the constraints of the OJEU advert. However, the contract variations require negotiation with the supplier to be achieved. The change process therefore lacks competitive tension and has the potential to create disputes. The continual tension between the contract profitability and client requirements often act as a stumbling block to delivering timely change. It also places a considerable burden on ECC officers to contain cost increases and risk transfer attempts by the contractor.
Continuous improvement	5	Contract structure lacks continuous improvement incentives for the contractor. This situation exists because it is difficult to foresee future improvements and the accompanying financial rewards to be granted. This has resulted in a lack of continuous improvement over the existing contract life and has probably been exacerbated by the tension between changes that are beneficial for ECC yet reduce profit for the contractor.
In-house resource / deliverability	7	Retendering of existing contract is straightforward, however, the time remaining for this process is very tight and will result in the use of a restricted tendering procedure. The limited time will also constrain the number of changes to the existing contract. This means ECC has to commit to a fixed set of terms and conditions and risk profile without negotiation. This may adversely affect price or the number of bidders. Existing staff resources to manage the tender process and future contract management should be sufficient.
Risk management	8	Risks associated with this option are well understood as the service has been delivered using this model for over 7 years. Contract affords significant risk protections for ECC . However the risk profile comes at a price. The private sector will add a significant premium for the current risk profile and have indicated during market testing they lack appetite for the existing risk profile.
Market appetite	4	Contract scope and value is large and risk appetite in the market has deteriorated. Circa four bidders identified during soft market testing which does not give high-level of confidence in keen price competition. Use of the restricted procurement procedure may be unattractive to some suppliers if the risk profile written into the contract is not aligned to their business objectives.
Overall Score	**44**	

	Option B (Dissaggregated outsourced)	
Evaluation Criteria	**Score**	**Rationale**
Future financial savings	6	This option is more difficult to achieve than Option B due to the disaggregated nature of the contracts. In option B, one contractor is able to drive efficiency and savings through the entire supply chain, whereas in this option the authority will need to negotiate with each party and ensure that any interfaces are managed/delivered. This reduces the chances of success and increases the costs of delivery. This option will also require greater ECC resources as multiple procurement processes will be needed.
Customer service	6	Additional interfaces (between contracts) are created by this option that may result in difficulty for ECC contract management team to fully recover costs arising from service failures.
Control / flexibility	6	Likely to have the same limitations as Option B for complex changes as the change process is likely to affect multiple contracts and will always lack an element of competition. Simpler changes may be more efficiently delivered by this option.
Continuous improvement	4	Contracts are likely to lack continuous improvement incentives for the contractor. This situation exists because it is difficult to foresee future improvements and the accompanying financial rewards to be granted. Having a number of specialist contractors in this model means that ECC should benefit from continuous improvement within their respective areas. Where this becomes more complex than Option B is in delivery as the interface risk between the various suppliers may prevent the improvements from being delivered.
In-house resource / deliverability	5	Requirement to produce multiple sets of tender documents and to resource multiple procurement processes in a short space of time will be challenging. More contract management resources would be required as the contract interfaces need careful control. This approach will be a bigger drain on internal resources than option B as there will be multiple contracts to deliver and manage. With an increased number of parties and interfaces between them, changes to the service can be more challenging to deliver and may require more negotiation than dealing with a single contractor.
Risk management	6	Disaggregation of the services creates multiple contract interfaces to manage. These can become complex in unforeseen circumstances and therefore carry more risk for ECC than Option B.
Market appetite	8	Splitting the services into multiple contract areas will attract new entrants into the market and will allow smaller businesses to compete. This will improve price competition and will help to remove interface profit margins.
Overall Score	**41**	

	Option C (Hybrid Sourcing)	
Evaluation Criteria	**Score**	**Rationale**
Future financial savings	7	Many of the savings achieved will be fully realised by ECC for example: avoidance of private sector profit margins; any future reduction in staffing numbers; recyclate income upsides; and waste tonnage reductions. Some savings may not fully benefit ECC as the bulk transport element remains outsourced. In a future re-procurement scenario, this option could have significant negative future financial impacts as harmonisation of transferring employee terms and conditions with ECC's will have occurred and these cannot be unpicked.
Customer service	8	Opportunity to improve customer service wherever ECC prioritises (through use of own staff). This option removes the issue of contractor distraction caused by increasing profits over customer care. Challenge remains to manage and motivate own staff, however, this is to be addressed through early and ongoing consultation/engagement with the workforce. This option also provides the opportunity to be more responsive to issues as these will be dealt with directly.
Control / flexibility	8	ECC control over main labour element brings inherent flexibility. Ownership of RoRo fleet and containers will also enable changes to the size of the service to be made without contractual penalties. Much of the service configuration can be altered without the need to re-negotiate contract terms. Changes will however still be subject to ECC governance processes and will also be somewhat constrained by the outsourced interfacing arrangements.
Continuous improvement	8	Prospects for service improvements are good including increased potential for third sector involvement in service delivery. However, improvement concepts have to be generated by ECC team and may be limited by budgetary constraints. This option provides a greater level of opportunity for ECC than Options B and C because improvements that are attractive to ECC are not necessarily attractive to the contractor.
In-house resource / deliverability	6	Service area lacks previous experience of bringing waste management services in-house. Additional resources will be required (HR; Legal etc) to support the successful transition/delivery of this option. Prospects of securing the necessary resources during the operational phase are good because most staff required will transfer to ECC under TUPE arrangements.
Risk management	4	Risk transfer under this option is high i.e. most service delivery risks sit with ECC such as ultimate Health and Safety responsibility, any union/staff issues, impact of negative movement in recyclate market pricing and full impact of increases in labour costs.
Market appetite	8	Bulk haulage, materials marketing and plant/equiment will be tendered. The markets in these areas are strong and will result in healthy competition and good prices.
Overall Score	**49**	

2.3.4 The main weaknesses of the fully integrated outsourced model (Option A) are the private sector profit margin applied to a significant proportion of the contract (labour); the lack of an effective continuous improvement mechanism; and the lack of private sector appetite for taking recyclate marketing risks. Disaggregating the service elements into separate contracts (Option B) is likely to go some way to addressing these shortcomings, however, it will not overcome the private sector profit margin downside and it creates additional contract interface risks that will sit with ECC.

2.3.5 Market engagement highlighted that suppliers view on risk has changed significantly since the current contract was let in 2013. Providers are not prepared to take a risk on market price for recyclates, volumes of recyclates, indexation and fuel costs. Therefore, it is highly likely that ECC will be fully exposed to the cost of these if they materialised.

2.3.6 Option C results in the highest level of risk transfer to ECC, however, it brings a number of important potential upsides including opportunity to benefit from: more control over the processes that could reduce residual waste tonnages; positive movements in recyclate pricing; any synergy savings. The most significant attractive feature is the removal of the private sector profit margin on several of the service elements including the labour element which forms over 50% of the IWHC expenditure.

2.3.7 One of the most apparent risks created by Option C relates to the potential transfer of staff from the Contractor to ECC under the Transfer of Undertakings (Protection of Employment) Regulations (TUPE) and the associated costs. Such staff transfers may lead to increases in employer liability costs. While the contract does require the Contractor to provide ECC with specified employee information to ECC when requested, the final employee liability information may not be received until 28 days prior to transfer (the timeframe specified by TUPE).

2.3.8 Option C achieved the highest overall quality score of 49 out of a potential 70 quality points.

2.4 Quantitative Evaluation

2.4.1 The quantitative assessment provides an evaluation to assist the operational and value for money decision.

2.4.2 It considers an OJEU procurement for an integrated contract and an in-house run service considering the use of public capital.

2.4.3 The model to review the approach has been designed to meet the following approaches:

- to ensure that the simplicity of approach reflects the early point at which this analysis takes place;
- to focus the ECC's attention on the underlying assumptions and the interplay with qualitative judgement;
- to reduce costs and ensure that ownership of the decision lies with ECC;
- follows the principles in the Green Book to introduce consistency across the public sector and improve the underlying evidence base.

2.4.4 A summary of the quantitative evaluation and the results can be found in the confidential appendix: Table 1.

3 Risk Mitigation

Whilst Option C is the preferred option, it still carries several risks for ECC. Table 3 outlines the key risks identified and the proposals to reduce the risks to acceptable levels.

Table 3: Risk Profile

Risk	Probability	Mitigation
Fuel price increases: ECC will pay actual price on these costs	**Medium**	Accept and monitor pre-procurement. Review alternative fuel options. Seek to improve plant and vehicle efficiency.
Increased cost of the workforce through any harmonisation in respect of contractual terms and natural turnover of staff.	**High**	Where possible this risk is included in the financial modelling. However, this is subject to further validation through due diligence.
Recyclate price fluctuation:	**Medium**	As ECC will be taking on the entire basket of recyclates, the potential for adverse movement in all items simultaneously is low. For example, the basket extends to cover traditionally income generating items such as non-ferrous metals, with cost items such as plasterboard. ECC plans to enter a contract with a waste management company or broker to which incorporates a gainshare mechanism to reward the contractor where prices are preferable over agreed indices. This will assist in further mitigating ECC's exposure.
In situations where the service has to be re-tendered in the future, should there have been any change to employment terms resulting in elevated pension costs, salary costs or other staff-related costs, these would persist and could impact the attractiveness of the service to the market.	**High**	Accept. Ensure decision making process through Cabinet to select Option C is robust and includes a proper assessment of the financial implications of re-tendering. .
RCHW service is highly visible and therefore any employee relations matters which arise could cause reputational damage	**Medium**	Use ECC ODP expertise to ensure early engagement with staff and dialogue to understand issues. Financial modelling for Option C includes 2 Full Time Employees for Human Resources to support the business directly. Further employee matters and considerations are highlighted in paragraph 4 below
Local Government Reform leads to changes in the Essex	**High**	All future options are vulnerable to this risk. Option C is however less exposed

Risk	Probability	Mitigation
Waste Disposal Authority organisation in terms of geographical scope and/or powers.		as the outsourced elements are of smaller total value and changing the contracts to match any new organisational structure therefore carries less financial risk than a fully outsourced service. Controlling the majority of the labour force also creates more opportunities in terms of integration.
Without sufficient internal resources the Hybrid Sourcing Model would struggle to be delivered.	**Medium**	Internal resources have been requested to deliver Operational Insight, ODP advice and Project Management support. This will also be reviewed and considered throughout implementation.
Pending changes in national legislation for example; to issues such as extending to issues such as extended waste producer responsibility	**Medium**	Flexibility built into Hybrid Sourcing Model (Option C) to allow efficient solutions to support changes.
Covid 19 and Brexit may impact International Supplies requiring longer lead in times for mobilisation.	**Medium/High**	Plan currently allows six months for mobilisation period for Plant equipment. However, if this lead in time is impacted ECC will investigate leasing options for an initial period to ensure continuity of service. This will require planning and will have further financial implications.

4 Employment and People Implications

4.1 If the recommendation to insource services as outlined within the Hybrid Sourcing option is taken there are a number of significant employment and people implications to ensure compliance with the Transfer of Undertakings (Protection of Employment) Regulations 2006 Regulations, and to ensure risks and opportunities are effectively managed.

4.2 ECC would need to inform the appropriate representatives of the affected employees of the transfer of any measures proposed and would need to consult on any proposed measures. Certain specified information would need to be provided to the representatives long enough before the transfer to enable the outgoing employer to consult with them about it.

4.3 If there are any changes or proposals for changes following the transfer, these "measures" would have to be discussed with the representatives of the affected employees. The incoming employer is required to provide the outgoing employer with information on proposed measures to allow the outgoing employer to comply with its duty to inform and consult. There is no set timetable for consultation, but it must be in "good time" before the transfer, and the larger the transaction and the more staff affected, the longer the timetable will need to be.

4.4 TUPE provides that all the transferor's rights, powers, duties and liabilities under or in connection with the transferring employees' contracts of employment are transferred to the transferee. This grants rights under the contract of employment, statutory rights and continuity of employment and includes employees' rights to bring a claim against their employer for unfair dismissal, redundancy or discrimination, unpaid wages, bonuses or holidays and personal injury claims. Any dismissals will be automatically unfair, where the sole or principal reason for the dismissal is the transfer. Dismissals may not be automatically unfair where the dismissal is for an economical, technical or organisational reason (ETO) requiring a change in the workforce. This ETO defence is narrow in scope and must entail changes in the workforce, e.g. job functions, workforce numbers.

4.5 Conceptual designs have been completed in terms of what (if any) additional roles would be required to support the recommendation. Although any final recommendations would need greater detail in terms of any current team structures, this detail may not be available until the due diligence stage (far closer to the actual TUPE date). This could present a risk around the amount of time to validate and progress any new posts before individuals would formally TUPE in. Financial modelling has included two full time employees for ODP to support the implementation of the TUPE and service integration.

4.6 The natural turnover of staff following insourcing may result in inconsistent terms and conditions within the service, that could result in possible equity claims and impact on how attractive this service would be to market, should there be a desire to spin out into a contractual model in future. The insourcing of this workforce could make any future procurement activity less attractive to the market if the workforce was brought onto ECC terms and into the Local Government Pension Scheme. This could happen through a harmonisation of terms or through natural turnover. Therefore, this would not be a recommended option if we have any intention to go back out to tender with the market in the short to medium term.

4.7 Information and consultation failures can result in joint and several liability between the outgoing and incoming employers, although the contract governing the transfer can cater for apportionment of liability here. A failure to comply with TUPE could expose ECC to potentially large claims.

4.8 Whilst the staff costs associated with the recommended option have been modelled, as we are not yet in due diligence, we cannot be clear on the current or future liabilities, which remains a risk. This includes costs associated with contractual terms which are both written and implied. There could also be an additional cost to integrate this workforce and their terms onto our current systems, previous changes have come with considerable cost and have had long lead in times, however this detail cannot be provided until further information is available