

PROCUREMENT OF WASTE AND RECYCLING SERVICES IN THE UK LESSONS FOR NEW ZEALAND

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Introduction

Procurement of waste and recycling services is one of the most important and financially significant decisions that a Territorial Authority (TA) is likely to make in respect of waste management. Determining how those services are designed, and how they are procured, is therefore critical to good waste management.

The delivery of waste and recycling services through contracts is where policy and waste management and minimisation planning are translated into reality. In the wider scope of strategic objectives, there is a real challenge to ensure that contracts facilitate rather than hinder moves towards sustainability. ‘Waste management’ can no longer be achieved by signing a contract to have rubbish collected and taken to a landfill – the variety of waste streams that require specific collection and treatment options are ever-increasing and this is key to improving New Zealand’s performance on waste reduction and diversion from landfill.

When considering the best way that waste management services can be procured, it is a good start to understand why TAs choose to contract out services in the first place.

Current practice is for the majority of waste services to be contracted out – few TAs still provide rubbish and recycling collections solely through in-house or council-owned operators. However going back 20 years or less, the situation was the reverse and the majority of services were provided directly.

The waste management industry has in fact oscillated between contracting and in-house service provision before – one of the earliest examples being a contract for ‘dust removal’ in central London¹ in 1824. 40 years later, the service was taken back in-house and the Council developed a number of facilities, a vehicle fleet, and other assets. In 1988 the service was again contracted out alongside operation or provision of infrastructure.

Varied influences have brought us to a time where most services are contracted out, including:

- **Privatisation** – in the mid-80s there was a shift towards privatisation in many western countries. In New Zealand this was encapsulated in ‘Rogernomics’ and the drive towards privatisation that entailed². In the UK, this was further enforced through mechanisms such as the 1988 introduction of ‘compulsory competitive tendering’ where in-house service providers had to bid against private suppliers³⁴

¹ Westminster – initially Paddington Borough Council, now the City of Westminster

² <http://www.commondreams.org/views/081500-106.htm>

³ Frederick, D (1994) “*Why Compulsory Competitive Tendering for Local Government Services is not as good as Privatisation*” Economics Notes No. 52

- **Cost** – competitive tendering should theoretically reduce overall costs to the local authority, with nominal savings of around 18% recorded in the UK⁵⁶
- **Waste Reduction** – services are no longer as simple as the householder placing a receptacle out for collection, the contents being removed, and transported to a final disposal site – and so specialists are more often required
- **Technology** – the variety of treatment technologies available means that there is no longer one ‘best’ way to treat a waste stream and it is rare that a local authority waste officer has sufficient technical knowledge to identify the best option
- **Risk** – it is usually assumed that contracting out services puts the local authority at a remove from financial, health and safety, and market risks⁷

It would benefit all of us in the waste sector to review our assumptions on these issues, consider to what extent they still hold true, and whether the service delivery models in use are still the most appropriate given the continually evolving waste management landscape. Many of us have no doubt had the experience of a contract being ‘bought’, and the ensuing bombardment of contract variation requests. In extreme cases, the local authority may have to choose whether to allow their contractor to fail through poor finances, or to ‘bail them out’ in the interests of continued services. TAs also need to ensure they are fulfilling their role in monitoring health and safety compliance – otherwise they are just as liable as the contractor should something go wrong. Whilst it is fairly easy to demonstrate nominal savings gained through competitive tendering in waste contracts, once the cost of the procurement process is taken in to account the net savings are often minimal – just a few examples of common assumptions failing to hold true.

Waste management is increasingly becoming an environmental career rather than a technical engineering one – a quick scan of international tertiary courses in waste management will demonstrate this. The role of the public sector waste manager now requires skills in partnership building, contract management, and service delivery; and the focus is less on the technical and engineering skills that were in demand 20 to 30 years ago.

These various shifts in the waste management sector should therefore be reflected in the way that we procure services and the forms of contract that are used. In New Zealand a waste management service contract is usually an adapted version of a civil engineering contract⁸ although the MfE’s *Guidance Principles: Best Practice for Recycling and Waste Management Contracts* (2007) notes that this has “shortcomings for waste and recycling contracts”. This raises a number of questions:

- why are many TAs still relying on a contract form that is not designed for our industry, when it is becoming less and less relevant and requires so much adaptation to be used?
- Is the way the sector has become used to procuring services in New Zealand necessarily resulting in the best outcomes? and

⁴ Szymanski, S (1996), “*the Impact of Compulsory Competitive Tendering on Refuse Collection Services*” Fiscal Studies 17 (3)

⁵ Chaundy, D and Uttley, M (1993) “*The Economics of Compulsory Competitive Tendering: Issues, Evidence and the Case of Municipal Refuse Collection*” Public Policy and Administration, 8 (2)

⁶ Szymanski, S and Wilkins, S (1993) “*Cheap Rubbish? Competitive Tendering and Contracting out in Refuse Collection*” Fiscal Studies 14 (3)

⁷ The recent experience in Christchurch would suggest otherwise.

⁸ NZS 3910 - Ministry for the Environment (2007) “*Guidance Principles: Best Practice for Recycling and Waste Management Contracts*” working draft available at www.mfe.govt.nz

- Are our assumptions still valid as to what those ‘best outcomes’ might be?

The UK Waste Management Sector

The authors both have recent experience of TA waste service procurement practices in the UK, and have noted the differences to NZ practice. In the UK, much wider variation has developed in the way that waste management services are procured and the forms of contract that are used. These forms of procurement are, in large part, responses to what is an increasingly fast changing and fluid waste management landscape. By discussing some of these forms of procurement and contracting that are uncommon in New Zealand, we hope to answer some of the questions raised above, and provide food for thought leading in to your next procurement project.

It is outside the scope of this paper to provide an in depth analysis⁹, but two of the relevant key features that waste operators must respond to include the following:

- **National waste minimisation** targets that are devolved to TAs: this means that performance in terms of waste minimisation is a key feature of any contract – making ‘output’ based specifications and integrated contracts more logical.
- **Landfill Allowance Schemes** limiting the quantities of biodegradable municipal waste that can be landfilled. Diverting biodegradable waste (organic waste) means that capital intensive facilities must be procured, and the payback on such facilities requires long contract timeframes.

Traditional Procurement and Contracts – where we have come from

The practices that have become common in New Zealand over the last 10 to 20 years are what we outline here as the ‘traditional’ process¹⁰. This is essentially what is described in the MfE’s Guidance Principles.

The procurement process typically begins with the local authority working through some kind of planning and consultation process to agree the basic parameters and scope of the service(s) to be provided. Some kind of tender document will be written, usually comprising a standard ‘front end’ for general conditions, with a specifications ‘back end’ where the service parameters, performance management, payment mechanisms, and other terms and conditions are set out. An evaluation methodology will be developed and agreed.

The length of the contract for a collection-based contract will usually be 5 to 7 years; based on the premise that collection vehicles are usually amortised over that period. Other contracts, such as those for processing facilities and transfer stations, are often longer for a similar reason. Once responses to the tender process have been received, whether through a ‘request for proposal’, ‘request for tender’ or other process, the offers from the market will be assessed against the agreed evaluation criteria and a decision made.

This is obviously a very simplified description of the process, and within this there is potential for much variation and the inclusion of ‘partnering’ or ‘alliancing’ approaches - however the basic steps taken remain the same.

⁹ For more detail - the UK waste sector is the topic of a series of articles by the authors in Waste Awareness

¹⁰ Of course our earlier discussion of the history of contracting means that there is no such thing as ‘traditional’ – but this is generally the default option for most local authorities at the moment.

If the specifications section of the contract has been prepared thoroughly, the advantage of this approach is that the contractor can be held firmly to the terms of the contract and the relationship can be restricted to monitoring, performance reviews, and payment.

The disadvantage, as many of us will have experienced, is that it is next to impossible to consider all eventualities in the diverse services we offer today, and allow for these in the specifications. Therefore in most cases, the relationship between the contractor and the local authority inevitably involves an amount of negotiation and agreement to resolve how these unforeseen issues are dealt with. The increasing complexity of waste management services means that this is happening more and more, leading to the emergence of terms like 'partnering' and 'alliances' with contractors rather than a more formal, strictly contractual, relationship.

This process is very similar to what is termed a 'bill of quantities' contracts in the UK. The specifications section of an average New Zealand contract, along with the prices bid by the successful tenderer, becomes the bill of quantities against which all services must be performed and charged for.

In years gone by traditional contracting approaches met the needs perfectly adequately where services were relatively well defined. Nowadays however 7 years is a long time in waste management. After a couple of years of a contract, changing priorities, an increasing focus on waste minimisation, and the development of new technologies could mean that the original requirements have varied beyond recognition.

Where a local authority and their contractor have a good relationship and both follow a partnering approach, this doesn't necessarily cause a problem. However as soon as either party challenges the other, the lack of a detailed agreed service specification and charging arrangement leaves both in a weak position and often days of searching through emails and paperwork will follow before a resolution is reached.

Alternative Procurement Processes

Public procurement processes in the UK are extremely tightly controlled by the Government and by European Union Rules. The four methods available for waste management contracts are open, restricted, negotiated, and competitive dialogue procedures.

- **Open:** the procurement process is similar to the traditional tendering process described above. Any organisation able to provide the services requested submits a form of tender document, and the award of the tender is made based on prepared assessment criteria, in which price usually features strongly.
- **Restricted:** similar to above, except that an initial selection process is carried out through a pre-qualification questionnaire or similar, and only those selected potential suppliers can submit a tender.
- **Negotiated Procedure:** negotiations are carried out with a number of potential suppliers to agree the details of the tender conditions. This procedure can only be used in certain circumstances, and is subject to careful regulation to ensure that competition is still achieved.

Negotiated Procedure procurement processes can be advertised or not. If advertised, the advertisement has to be placed in the Official Journal of the European Union (OJEU) inviting expressions of interest. In the latter, the local authority selects the suppliers they want to negotiate with, as long as there are a minimum of three (or less if you can't find more than three potential suppliers).

The negotiation process suits situations where the specifications are strongly outputs based, and services could be delivered in a number of ways. They are also used when the potential suppliers are likely to be extremely limited, and the specifications can not be agreed with negotiation with potential suppliers.

- **Competitive Dialogue Procedure:** this is a new procedure introduced in the UK in 2006 and can only be used in certain situations¹¹. Similar to 'negotiated procedure' but more structured - this is suited to complex contracts where the local authority and the potential suppliers both benefit from having detailed discussion of the proposed service or facility (for waste management procurement) before the contract is awarded. It is useful where a local authority can define the outputs they are aiming for, but a wide range of potential solutions are available or they are not sure how best to achieve the outcomes; for example, a local authority may wish to divert 20% of their waste from landfill. The myriad options for achieving this could then be discussed with prospective suppliers through the 'competitive dialogue' procedure.

The aim of competitive dialogue is to allow the local authority to select suppliers with the most potential, and discuss their needs and requirements with only those suppliers with the intention of identifying solutions or further defining their specifications. Several stages of 'dialogue' can be carried out, progressively narrowing the field.

At some stage the suppliers are asked to submit their proposed solutions in writing, and this forms the basis of the contract document. Post-tender negotiation is very limited under this process, so it is important that the written proposals are comprehensive and reflect the discussions held with the local authority. Legally the most 'economically advantageous' written proposal or tender must then be accepted. By definition, this tender will meet the requirements of the contracting authority as a result of all the prior discussions and so where two potential suppliers arrive at the same solution, the cheaper or 'MEAT'¹² tender should be chosen.

Competitive Dialogue procedures are commonly used with Private Finance Initiative (PFI - a form of public-private partnership) projects.

Most waste management contracts in the UK until the last five years or so were procured through the open or restricted procedures. These are more traditional procurement routes, while the negotiated and competitive dialogue procedures reflect the changes in the waste market by encouraging open discussion and formal partnering-style approaches.

Alternative Forms of Contract

There is a similar level of variety in the UK when it comes to forms of contract, ranging from long term, formal partnering contracts to short term strict specification-based contracts. Here

¹¹ Office of Government Commerce (2006) "*OGC Guidance on the Competitive Dialogue Procedure in the new Procurement Regulations*" available on www.ogc.gov.uk

¹² Most Economically Advantageous Tender is often referred to by the acronym MEAT

we discuss some innovative examples of different contract forms and what advantages they can have in the current waste management environment.

Public-Private Partnership Contracts

One of the earlier examples of a long-term, truly partnering, contract in the UK was the ‘3rd generation’ contract between South Gloucestershire Council and United Waste Services¹³. This contract was a full facility contract delivering all waste management services, and was also one of the earlier PFI contracts agreed – signed in July 2000, for a 25 year period. The contract specifically provided for an in-vessel composting facility by 2008, 2 transfer stations and 2 recycling centres, along with collection services which were to be reviewed at least every five years.

South Gloucestershire Council worked with a not-for-profit sustainability organisation, Forum for the Future (FFTF), who specialise in sustainable procurement. The ‘3rd generation’ contract was a part of FFTF’s ongoing procurement work, and their role was to help the Council identify criteria to choose a long term partner rather than a service specification approach with the lowest price accepted¹⁴.

Private Finance Initiatives

BOOT (build, own, operate, transfer) and DBO (design, build, and operate) contracts are quite similar to the long-term public-private partnership contracts that are becoming more common in the UK, especially where private PFI funding is involved. At the end of a BOOT contract, the ownership of the assets involved transfer back to the local authority.

The advantage of these contracts for a local authority is the private sector investment that can be accessed, based on the certainty of a long term consistent income. Contracts can be very tightly specified, or can be more outputs based in which case the private sector is asked to propose their favoured technology to achieve the outputs required.

To attract reasonable investment from the private sector, BOOT and similar styles of contracts need to be longer than most current waste management service contracts. In a recent New Zealand example Auckland City Council and Manukau City Council signed a 14 year BOOT contract with Visy. In the UK, it is not uncommon for these types of contracts to be 25 years or even longer.

One risk with a contract of this nature is that the councils involved are essentially confined to the technology that’s chosen when the contract is tendered. Although some variation can be allowed for in the contract documents (such as modifications to allow the inclusion of new materials in a MRF) the basic technology remains the same and this also dictates the collection methodology used.

It can also be a risk to enter in to a contract based on a technology that has not been proven locally, and so the technologies involved in these contracts have usually been in use for some time and are no longer at the cutting edge of innovation.

Cost-plus

¹³ Soon after the contract was awarded, UWS were bought out by SITA UK (although both were owned by Suez at the time).

¹⁴ www.forumforthefuture.org.uk

These are a relatively new form of contract in the UK. When TAs are looking for value for money, flexibility, variety and responsiveness in their full-facility contracts, an arrangement where the contractor is paid per service or visit is not conducive to achieving efficiencies and so often these contract forms evolve into a 'cost-plus' arrangement.

The theory behind cost-plus contracting is that the local authority accepts that they are employing a profit-making business, and therefore pay the true costs of providing the service plus an agreed profit margin. In return, the contractor must provide access to their accounting records and an open-book approach is maintained. The TA has complete control over how their funds are spent and prioritised, and alterations to the allocation of funds can be made quickly as the needs of the community changes. An external auditor is usually involved who will check prices against the market. In many cases, if the contractor is found to have prices higher than the general market, adjustments will be due to the local authority and back-dated as far as necessary.

A contract manager at a local authority working under this type of arrangement needs to have a good understanding of the practicalities of providing waste management services, and the ability to carry out a 'common sense' check of charges from the contractor between audits (although as noted adjustments can be backdated). A contractor delivering a cost-plus contract needs to have the capability and experience for a wide range of services and perhaps as a result, most cost-plus arrangements are with larger companies that have the ability to support their regional offices with expertise and specialists as and when required. In some cases, the local authority and their cost-plus contractor are co-located in offices – improving partnership working, transparency and responsiveness further.

Council-Controlled Organisations¹⁵

The final point mentioned for cost-plus contracts demonstrates how for some TAs, contracting is almost coming full circle with services being delivered on a reactive basis and closely managed in-house. Some TAs in New Zealand have short-cut that circle, and still provide services through a business unit or directly in-house. There are a range of options, with varying levels of management and financial involvement in the operation of the organisation involved.

Council-controlled organisations (CCOs) can be for-profit or non-profit, but the TA must have a controlling share in the organisation, whether through voting rights or management. A council-controlled organisation which is intended to make a profit is termed a Council-Controlled Trading Organisation. The advantages of in-house services, or a CCO, are similar to those of a cost-plus arrangement, with the added responsibilities of health and safety, staff management and maintenance of vehicles and facilities.

Transwaste Canterbury Ltd, operating the Kate Valley landfill, is a good example of a council-controlled organisation where the 'council' holding a 50% share is in fact a group of local authorities from the Canterbury Region.

The Royal Commission review of Auckland region governance recommended that waste management for the new Auckland Council would be best delivered through a CCO¹⁶.

¹⁵ Formerly known as LATEs – Local Authority Trading Enterprises if for-profit. Non-profit organisations included trusts and incorporated societies.

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www.royalcommission.govt.nz/web/part4/21_council_organisations_and_council_controlled_organisations.html

There is little public appetite for local authorities to provide perceived ‘high-risk’ services or facilities through such a direct relationship such as a CCO, and councils are also seen as being poor at achieving commercial objectives and at making a profit. This perception could make life difficult for a TA that is keen on a more unusual waste management solution but also wants to retain the control and flexibility that a CCO arrangement provides – and often they may end up in a BOOT or design-build-operate arrangement instead.

The changing New Zealand Waste Management Landscape

Various recent government initiatives are contributing to the rapid state of change in the waste management sector, including:

- **The newly-enacted (September 2008) Waste Minimisation Act 2008** has created a new legislative environment for the management of waste - including the imposition of the waste levy.
- Further drivers for change in the sector are also expected from the revision of the **National Waste Strategy targets**, which are expected to be announced towards the end of 2009.
- The introduction of a **NZ Emissions Trading Scheme** which will impose a cost on waste disposed of to landfill (although the mechanism for this is not yet determined); and
- The possible intention by central government to introduce National Environmental Standards on waste disposal facilities (including cleanfills).

TA budgets are also under extreme pressure in this economic climate, and there is increasing incentive to seek efficiencies from all waste management services. The overall effect of all these changes is likely to be an increase in disposal costs, which will incentivise diversion and require higher standards of planning and management of services to achieve cost reductions. The role of procurement in achieving these various imperatives will mean a stronger focus on strategic and long term implications, with services having sufficient flexibility to meet changing demands over a contract’s life.

TAs will need to consider following types of service requirements:

- Increasing the variety and quality of materials collected for recycling/recovery
- Ensuring long-term viable markets exist for collected materials
- Establishing or expanding processing capacity
- Transfer of resources between contracts
- Meeting government or locally established waste minimisation targets
- Ensure efficiency of service delivery
- Meeting ever-increasing householder expectations
- Ensuring health and safety of workforce
- Controlling administrative costs and resources
- Ensuring risk is allocated efficiently (i.e. to where it is most effectively managed)
- Managing service changes

New approaches to procurement arrangements are clearly required to meet the new challenges. It is our view that, taking a lead from some of the approaches we have observed in the UK, these new approaches will need to look to arrangements that more closely align the interests of the service provider and the customer (council/ratepayer).

Key aspects of this new approach could include:

- Integrated contracts, allowing the transfer of resources between diversion-related elements and disposal-related elements
- Including certain infrastructure in integrated contracts, such as transfer and resource recovery facilities and even potentially processing facilities
- As a result of the complexity involved in integrated contracts; relatively long contract cycles are likely to be more sensible, particularly where infrastructure development is involved and longer periods are required to amortise capital investment¹⁷
- Longer procurement cycles make flexibility in the contract an imperative, given the changes that can occur in waste management over a small number of years
- Contracts must be structured to enable flexibility while also aligning the interests of the different parties so that everyone works to achieve the same outcomes – contractors need to benefit from achievement of council objectives by including waste minimisation, service quality, ratepayer satisfaction etc. as KPIs tied to financial incentives.

Summary

We are no longer operating in a waste management sector where a contract can be simply specified and tendered. Waste management services have moved far beyond kerbside rubbish collections – there is now a bewildering and ever-increasing array of potential technologies available, and individual waste streams are identified that each need specific services and treatment. It will be a rare local authority waste manager that will have all the experience and knowledge required to identify the best solution possible for their community extending many years in to the future.

Longer term, partnering style, contracts focused on specifying outcomes rather than services can put the task of designing the best package on to the private sector, with the ability of the company to deliver and manage waste services the basis of awarding contracts rather than the lowest price for a set requirement. Procurement processes are less frequent, although there is a higher risk in signing up with a partner for a lengthy period – during which time the partner themselves could change significantly.

The reasons why local authorities began to contract out services 15 to 20 years ago are no longer so applicable. The financial risk has demonstrably not been removed from the local authority, and health and safety legislation makes the principal of a contract liable as well as the immediate employer.

It is timely for the public sector in New Zealand to rethink the reasons for contracting out our services in the first place, and consider whether a very different approach could achieve a better result in waste management and in financial performance, now and in the future.

¹⁷ In the UK typical integrated contract periods are 14 years (two vehicle replacement cycles) and longer