

2018/19 Budget

SUMMARY

This report sets out the 2018/19 budget proposal for consultation with boroughs

RECOMMENDATION(S)

The Authority is asked to:-

- 1) Note the 2018/19 budget for consultation with boroughs
- 2) Note the indicative Pay As You Throw (PAYT) rates in section 14 and resulting PAYT levy of £47.6 million
- 3) Note the Fixed Cost Levy (FCL) of £12.2 million in section 15
- 4) Note the recommended trade waste prices in section 16 and delegated authority to the Treasurer to change these in year should the need arise
- 5) Note there are no new proposed capital budgets in section 17
- 6) Note the target level of reserves of £4.2 million to act as a buffer for managing risks and avoiding supplementary levies, in section 18

1. Introduction

1.1 The Authority is required to set an annual budget including levies and charges. It is also required to issue a demand to constituent boroughs by 15 February each year. This report sets out the 2018/19 draft budget which will be subject to consultation with constituent boroughs. Following consultation the final budget will be reported to the January meeting for approval. The PAYT and FCL charges will then be levied.

1.2 The 2018/19 budget incorporates tonnage forecasts received from boroughs and the spending plans received from Authority managers. The managers' spending plans have been scrutinised and adjusted following a budget challenge session held with the Chair, Vice Chair and Chief Officers on 17 November.

2. Executive Summary

2.1 The key message is that the total costs and overall levies (£59.8 million) proposed for 2018/19 are marginally lower than 2017/18 levels, despite inflation running at more than 4%.

2.2 The 2018/19 budget includes the purchase of transfer station sites (see confidential report later in today's agenda) and funding to deliver business plan objectives / projects as well as continuing to run business as usual operations.

3. Expenditure and Income

3.1 The table below sets out the 2018/19 budget and the movement from the 2017/18 budget. The latest 2017/18 forecast is also included to provide context and illustrate the current level of activity.

	2017-18 budget £ 000's	2017-18 forecast £ 000's	2018-19 budget £ 000's	Changes in budgets £ 000's
Costs				
Waste Transfer and Disposal	44,615	43,199	45,592	977
Depreciation	8,227	8,169	8,600	373
Financing Cost	5,059	4,973	5,566	507
Premises	4,288	3,826	2,571	(1,717)
Employees	1,653	1,726	1,803	150
Supplies and Services	1,317	1,134	927	(390)
Revenue Funding of Debt	0	0	684	684
Concession Accounting Adjustments	(3,449)	(3,994)	(4,065)	(616)
Total costs	61,710	59,033	61,678	(32)

Income				
PAYT Levy	47,360	46,408	47,636	276
FCL Charge	12,520	10,720	12,214	(306)
Total Levies	59,880	57,128	59,850	(30)
Other Income	1,830	1,879	1,828	(2)
Total income	61,710	59,007	61,678	(32)

Total (surplus)/deficit	0	26	0	0
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3.2 The budget headings are per our usual format for regular budget monitoring reports however there are two new lines for 2018/19.

3.3 Firstly the Concession Accounting Adjustments have been separated out so the Waste Transport and Disposal and Financing Costs now reflect what we actually pay contractors and lenders. For budgeting purposes it is also clearer to see what the accounting adjustment actually is, rather than netting it off with other costs (as we have to under accounting requirements for our annual accounts). This line is explained in section 11.

3.4 Secondly the revenue funding of debt represents a new activity next year. It is the cost of repaying the loans for acquiring the freehold for transfer station sites. See section 10.

4. Waste Transport & Disposal (WTD)

4.1 The WTD budget accounts for the majority of the Authority's budgeted costs. The 2018/19 tonnage forecasts from boroughs have been reviewed for reasonableness by Authority managers. The forecasts together with contract pricing information form the basis for the calculation of the 2018/19 budget.

4.2 The 2018/19 WTD budget is £45.6 million, an increase of £1.0 million or 2.2% resulting primarily from the impact of inflation.

4.3 Most contracts require annual pricing adjustments based on the movement in the RPIX (retail price index excluding mortgages). The assumption for RPIX for 2018/19 is 4.0%. This

is based on the September 2017 index (4.1%) and the governments Office for Budget Responsibility's forecast for RPIX for next year of over 4.0%.

4.4 The contract pricing in the major PPP contract has gone a long way to dampening the increase in waste transport and disposal costs. This is because a significant portion of contract waste sees no / very little price inflation under the terms of the contract.

4.5 Another key factor limiting the growth in waste transport and disposal spending is the slightly lower overall borough forecasts of tonnages, better reflecting the current level of waste. The 2018/19 budgeted tonnage is made up of the following materials:

Material	2017/18 Total Tonnes	2018/19 Total Tonnes	Change
Residual	412,224	409,006	(3,218)
Mixed organic	16,000	16,200	200
Green	51,795	49,038	(2,757)
Wood	21,297	19,850	(1,447)
Kitchen	28,075	32,527	4,452
Other	13,661	12,252	(1,409)
Budget 2018/19	543,052	538,873	(4,179)

5. Depreciation

5.1 The budget for 2018/19 of £8.6 million is £0.4 million higher than in 2017/18. This reflects the outcome of the property valuation for the last audited accounts where full property valuations were undertaken by independent surveyors and the values increased – hence an increase in the depreciation.

5.2 The largest element of depreciation relates to the SERC and totals £8.1 million. It should be noted that for depreciation calculations, the SERC has to be separated out into its main components and each key component has to be depreciated over its own expected life.

5.3 The value of the SERC is £194.2 million and components are depreciated over periods up to 23 years.

5.4 Depreciation for the remaining assets have been calculated using the latest audited accounts and subsequent change in the asset registers.

6. Financing

6.1 The financing costs have increased from £5.1 million in 2017/18 to £5.6 million for 2018/19 primarily as a result of the acquisition of transfer station sites.

6.2 The largest component of financing costs relate to borrowing for the construction of the SERC and totals £5.0 million. The loans are at arm's length and from a borrowing perspective the boroughs are like any other lender with the loan agreements specifying the relationship with the Authority and including a rate of interest of 7.604%.

6.3 The budget assumes the transfer station sites will be purchased at the commencement of 2018/19 partly from borrowing and partly from utilising cash balances. The interest on this loan is budgeted at £0.6 million. Details for this can be found in the confidential report later in today's agenda.

7. Premises

7.1 The budget for 2018/19 of £2.6 million is £1.7 million less than the £4.3 million in 2017/18. The majority of this is due to the removal of site rents resulting from the purchase of transfer station sites.

7.2 Part of this reduction is offset in other budgets by an increase in Financing Costs and the new Revenue Funding of Debt.

8. Employees

8.1 The 2018/19 budget of £1.8 million is £0.2 million higher than the 2017/18 level. This is principally to allow for the delivery of business plan objectives, but also includes growth for inflation and pension contribution increases.

8.2 The establishment is planned to grow by 3.1 full time equivalent (FTE) posts from 31.3 to 34.4 FTEs. This provision for new posts relate to data projects (0.6), backfilling to deliver new office, IT and other projects (0.6), PPP contract audit work previously performed by auditors (0.4), reorganisation of site weighbridge work (0.5) and waste minimisation (1.0).

8.3 Putting this into context the Authority employed 88 FTE in 2012/13, 42 FTE in 2014/15 and over the last few years FTE numbers moving around at just over 30 focussed mainly on delivery of business as usual service. However with more complexity (e.g. financial management of the PPP contract) and a more ambitious business plan with a number of objectives and projects to deliver, appropriate resourcing will be required.

8.4 For projects, a decision to recruit will only be made if and when necessary, for example when projects are likely to progress beyond the initial feasibility stage.

9. Supplies & Services

9.1 The 2018/19 budget for Supplies & Services is £0.9 million, £0.4 million lower than the 2017/18 level.

9.2 The expiry of leases, £340,000 which now becomes the PPP contractor's costs and stripping out of unused fees (consultants etc.) of £62,000 account for the majority of the reduction in this budget.

10. Revenue Funding of Debt

10.1 The loan financing the purchase of the transfer station sites is a typical repayment loan. It is made up of two components – an element for the interest on the loan (see Financing Costs) and an element to actually repay the loan.

10.2 The Revenue Funding of Debt is the element to actually repay the loan and totals £0.7 million.

10.3 The report later in today's agenda details the implications of purchasing the transfer station sites on the cashflow, accounting and budgeting (section 7 and appendix 3 of that report). It explains that the site purchase is essentially the purchase of land and this has a different impact on the finances compared to the purchase other assets – resulting in this new line in the budget.

11. Concession Accounting Adjustments

11.1 Essentially under a PPP arrangement a contractor pays for the construction of an asset and then recovers it's investment over a long period through its operational charges to the local authority.

11.2 There are very specific and detailed accounting requirements that govern this type of arrangement. This is because the underlying nature of this transaction is that the local authority *essentially* owns the asset and the contractor is *essentially* a lender financing the construction of the asset.

11.3 The key feature of the accounting is the calculation of a concession accounting adjustment.

11.4 The concession accounting adjustments over the term of the contract were agreed with the auditors during the approval of the latest accounts. For 2018/19 they total £4.1 million, compared to £3.5 million in 2017/18. This reduces overall costs and levies by £0.6 million.

12. Growth and Savings

12.1 The majority of Authority spending is committed under long terms contracts (PPP) or agreements (loans) or governed by accounting requirements (depreciation). This leaves less opportunity for savings.

12.2 However, as part of the budget setting process at an operational level, a variety of measures have ensured a focus on savings across areas where managers are able to exercise some control. This included budget managers reporting their 2018/19 plans and proposed savings to a budget challenge session with the Chair, Vice Chair and Chief Officers.

12.3 The tables below identify the growth and savings included within the 2018/19 draft budget and separates out real growth and savings from other movements between 2017/18 and 2018/19 budgets.

12.4 Summary table:

	£ 000's
Budgeted levies 2017/18	59,880
Growth	2,587
Savings	(2,926)
Other movements	309
Budgeted levies 2018/19	59,850

12.5 Growth table:

Area	Explanation	Growth £ 000's
Waste Transport and Disposal	Pricing inflation on residual waste (£1,235k), haulage (£171k), food (£129k), green (£37k), increase in number of mattresses (£79k) and other tonnage movements (£12k)	1,663
Financing Costs	Growth reflecting interest payments on new borrowing to purchase transfer station sites (£639k)	639
Premises	Increase in rates (£62k), utilities (£10k), security services (£20k), and a range of other small increases (£13k)	105
Employees	New posts and reorganisations (£105k), inflation and increments (£37k), increase in pension contributions (£24k)	166
Supplies and Services	Rise in insurance premiums (£10k) and other minor items (£2k)	12
Other Income	Small reduction in other income (£2k)	2
		2,587

12.6 Savings table:

Area	Explanation	Saving £ 000's
Waste Transport and Disposal	Savings from wood and mixed organics procurements (£437k), optimisation of transport arrangements (£168k), reduced tonnages (£81k)	(686)
Premises	Removal of rental budgets (£1,775k), reduced SERC rates resulting from Suez negotiations with Valuation Office (£42k) and other minor reductions (£5k)	(1,822)
Employees	Reorganisation of Twyford management structure (£15k)	(15)
Supplies and Services	Expiry of leases with responsibility moving to contractor under the PPP contract (£340k) and stripping out unused consultancy budgets (£62k)	(402)
		(2,926)

12.7 Other movements table:

Area	Explanation	Increase / (Decrease) £ 000's
Depreciation	A full independent property valuation was undertaken and agreed with auditors for the last accounts. Depreciation has been calculated using the updated valuations (£373k)	373
Financing Costs	Reduction in SERC financing costs arising from timing of capital contributions (£132k)	(132)
Revenue Funding of Debt	Reflects the repayment of borrowing to finance the acquisition of transfer station sites (£684k)	684
Concession Accounting Adjustment	Per accounting requirements and agreed with auditors for the last set of accounts (£616k)	(616)
		309

13. PAYT / FCL split

13.1 PAYT costs relate primarily to waste that boroughs collect and deliver to transfer stations and FCL costs are those which relate to waste from HRRC sites and the Authority's running expenses.

13.2 Where directly attributable, costs are allocated to the PAYT or FCL as appropriate. Where costs are applicable across both PAYT and FCL (e.g. SERC depreciation relates to both HRRC residual waste and borough collected residual waste) these are apportioned based on the relative WTD tonnages in PAYT and FCL. The breakdown of the budget between PAYT and FCL activities is as follows:

PAYT	2017/18 £000's	2018/19 £000's	Change £000's
Waste Transport and Disposal	37,582	38,603	1,021
Depreciation (SERC)	7,001	6,955	(46)
Financing Costs (SERC/WLRWS)	4,430	4,288	(142)
Premises (SERC)	1,337	1,292	(45)
Concession Accounting Adjustment	(2,990)	(3,502)	(512)
PAYT Levy	(47,360)	(47,636)	(276)
Total	0	0	0

FCL	2017/18 £000's	2018/19 £000's	Change £000's
Waste Transport and Disposal	7,033	6,989	(44)
Employee	1,653	1,803	150
Premises	2,951	1,279	(1,672)
Supplies and Services	1,317	927	(390)
Depreciation	1,226	1,645	419
Financing	629	1,278	649
Revenue funding of Debt	0	684	684
Concession Accounting Adjustment	(459)	(563)	(104)
Non Levy Income	(1,830)	(1,828)	2
FCL Levy	(12,520)	(12,214)	306
Total	0	0	0

Note that the concession accounting adjustment has been separated out as detailed in Section 3.3.

14. PAYT Levy Income

14.1 The PAYT charge to boroughs relates primarily to the waste that boroughs deliver to transfer stations and is to cover the cost to the Authority for disposing of that waste.

14.2 The PAYT charge for 2018/19 is £47.6 million a small increase of £0.3 million or 0.6% from 2017/18.

14.3 The table in Appendix 1 (part 2 item) shows the proposed PAYT rates.

14.4 These rates represent the average cost to the Authority for the disposal of materials. They reflect the blended price paid to a number of contractors and for residual waste also the costs of the SERC.

14.5 These rates will be applied to the 2018/19 tonnage forecasts from boroughs and result in a monthly charge to them. Each quarter end a reconciliation exercise will take place to adjust for the actual amount of waste that each borough delivers, so boroughs only pay for waste actually disposed.

14.6 In addition to this, the Authority manages non-household waste from HRRC sites and incurs transport costs. On a similar basis the average transport charges for 2018/19 are provided in Appendix 1 (part 2 item).

14.7 Following harmonisation of transport operations during the current year, the transport charge for residual and organic collected waste for 2018/19 will be a blended charge.

14.8 Using tonnage forecasts from boroughs, the PAYT charges for 2018/19 are as follows:

Borough	2017/18 PAYT charge £000's	2018/19 PAYT charge £000's	Growth £000's	% Growth
Brent	8,922	8,882	(40)	(0.5%)
Ealing	10,627	10,084	(543)	(5.1%)
Harrow	5,946	6,383	437	7.3%
Hillingdon	8,480	8,557	77	0.9%
Hounslow	7,533	7,744	211	2.8%
Richmond	5,852	5,986	134	2.3%
Total	47,360	47,636	276	0.6%

14.9 It is worth noting that the above levies use borough forecasts for the volumes of waste, including any implications from service changes.

14.10 On this basis it is also worth repeating that should borough waste volumes be lower than they've originally forecast, then each quarter they will be refunded a sum to ensure they pay only for what is actually delivered. If their volumes are higher they will be asked to pay for the extra waste.

15. FCL Income

15.1 The FCL charge primarily relates to the cost of managing the treatment and disposal of household waste delivered to HRRC sites. It also includes the Authority's administration, nets off other income and includes a portion of SERC costs. The charge is set to recover all FCL costs and will be apportioned using the 2018/19 Council Tax base per the CTB (October 2017) returns provided by the boroughs.

15.2 The FCL charge for 2018/19 is £12.2 million which is a small reduction of £0.3 million or 2.4% from the 2017/18 level.

15.3 Using the 2018/19 Council Tax base, the FCL charge is as follows:

Borough	2017/18 FCL charge £000's	2018/19 Council Tax base	2018/19 FCL charge £000's	Change £000's	% Change
Brent	2,053	93,438	2,001	(52)	(2.5%)
Ealing	2,533	115,469	2,474	(59)	(2.3%)
Harrow	1,895	86,335	1,849	(46)	(2.4%)
Hillingdon	2,165	98,666	2,113	(52)	(2.4%)
Hounslow	1,893	86,219	1,847	(46)	(2.4%)
Richmond	1,981	90,157	1,930	(51)	(2.6%)
Total	12,520	570,284	12,214	(306)	(2.4%)

15.4 It should be noted that overall levies (taking both PAYT and FCL together) are marginally down from 2017/18.

16. Other Income

16.1 The 2018/19 budget is £1.8 million, almost identical to 2017/18. Trade waste income is the largest component at £1.2 million. We are conscious that the market trade waste prices, particularly for residual waste, are more competitive. Therefore for 2018/19 the trade waste prices have been reviewed with the intention of maintaining income by bringing in more trade.

16.2 The proposed main trade/DIY charges per tonne are provided below:

Type of waste	2017/18 £	2018/19 £
Trade waste residual and wood	195.00	160.00 for account customers and £165.00 for others
Trade waste recycling	97.50	80.00
Asbestos (Households only)	272.00	272.00
Mattresses (per mattress)	12.26	10.00
Bulky items	218.00	218.00

16.3 The effect of these price changes will be kept under review over 2018/19. Given the low value of trade income in context of the overall budget it is proposed that the Treasurer has delegated authority to take corrective action (i.e. change the above rates) should the reviews identify any risks.

17. Capital

17.1 Other than the capital budget for the purchase of transfer station sites, there are no new capital budget requirements for 2018/19. The budget for the transfer site purchase is detailed in the confidential report later in today's agenda.

17.2 It is worth noting the following capital budgets. These are balances on capital works still in progress which were previously approved by the Authority and will be rolled forward until completion or not required.

- Construction of a bulking facility at Victoria Road (£1.1 million)
- Twyford improvements (£738,000)
- Replacement Loading Shovel (£240,000)
- Contract Management Software (£30,000)
- New Head Office (£2.5 million)
- Replacement IT (£200,000)

18 Reserves

18.1 Reserves represent an organisations net worth. They provide a buffer for an organisation to manage risks, for example the fluctuations in the level of activity or costs – these variances in costs lead to surpluses and deficits being absorbed within reserves. On this basis, the Authority's approach to reserves has been to build up sufficient reserves to act as a buffer against risk.

18.2 The added benefit of reserves is that they can be used to stabilise pricing by removing the need for "in year" price reviews. For boroughs and indeed the Authority, this pricing stability / predictability facilitates better planning and budgetary control.

18.3 Identifying known risks facing an Authority provides a useful basis for determining a suitable level of reserves for managing risk. The specific risks and potential costs and likelihood that could be associated with them are as follow:

Risk Description	Likelihood	Financial Risk (£000's)
From time to time, a new market will emerge for recycling of specific waste streams (as opposed to landfill) e.g. carpets. The Authority tests and uses these markets cautiously, however these new markets carry a risk of both market and supplier failure. Should this arise there will be additional costs in making new arrangements to redirect and dispose of waste.	High	£300 (based on 2014/15 experience with mattresses)
Collapse of recycling markets leading to materials entering the residual waste stream	Medium	£200 (notional)
Whilst the contractor bears most of the risk in the event of the loss/closure of a transfer station, in major events like this there is a possibility of unforeseen additional costs in implementing and operating alternative arrangements. Therefore it would be prudent to set aside something for these uncertainties.	Medium	£200 (notional)
The budget is based on assumptions of indexation/ inflation, particularly in relation to contracts. There is a risk of higher costs due to higher than anticipated indexation/inflation	Medium	£500 (representing approx. 1% higher indexation)
With a changing market environment and in particular high inflation, procurement exercises could result in higher prices	High	£500 (representing 10% on key procurements in progress)
Increasing out of hours volumes and implications on service availability will lead to additional costs	High	£600 (based on pricing difference on 10,000 tonnes)
With a large number of competitors ready to receive trade waste, there is a risk that price competition could lead to a reduction in planned trade and DIY income despite more competitive pricing	Medium	£300 (representing 25% of trade income)
Purchase of transfer station sites doesn't happen in 18/19 meaning we'll still need to pay rent	Medium	£300 (representing the lost savings)
Risks / costs will arise from the complex PPP contract as a result of terms that are unclear or ambiguous in relation to the day to day operation and running of services.	Medium	£600 (based on contingent liability in last year's accounts)
Borough changes in waste collection services and changing social / demographics can have a significant impact and increase waste flows to HRRC sites. As these form part of the	Medium	£700 (representing a 10% growth in HRRC waste)

fixed cost levy there is a risk of extra costs that will need to be borne by the Authority		
Target level for reserves		£4,200

18.4 The target level of reserves for 2018/19 of £4.2 million is lower than the £5.6 million in 2017/18 primarily due to the removal of the risks in relation to SERC depreciation (£1.5 million) – the external auditors have agreed our methodologies and this risk has passed.

18.5 Ultimately, the level of reserves is a judgment based on the nature of risk facing an organisation and its risk appetite. On the basis of the risks identified above and appreciating that there are unknown risks which could materialise, £4.2 million represents a prudent and not overly cautious target level for reserves.

18.6 The forecast reserve position for the year ending 31 March 2018 is:

	£000s
Reserves available to manage risks 31 March 2017 per approved accounts	3,699
Forecast under-recovery for 2017/18 per period 7 budget monitoring report	26
Forecast position for 31 March 2018	3,725

18.7 Provided that no risks materialise and something close to the £3.7 million forecast reserve position is achieved for 2017/18, the Authority will have reserves slightly lower than the target level.

18.8 However, the gap is not significant and it is unlikely that all risks would materialise at the same time. Therefore at this stage there is no need to try and identify a means of building up reserves to the target level.

19 Financial Implications

19.1 The financial position and performance are provided in the report.

19.2 It is a statutory requirement for the Authority to set a balanced budget (Local Government Finance Act 1992) and to set the levy for constituent boroughs by 15 February (Joint Waste Disposal Authorities (Levies) Regulations 2006).

20 Legal Implications

20.1 There are no legal implications of this report

21 Impact on Joint Waste Management Strategy

21.1 The proposed Annual Budget has been set out in this report to demonstrate that the Authority is supporting the boroughs to deliver improved value for money to its residents in line with Policy 7

21.2 Policy 7: The West London Waste Authority and constituent Boroughs will seek to provide waste management services that offer good value, that provide customer satisfaction and that meet and exceed legislative requirements.

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