

NORTH LONDON WASTE AUTHORITY

REPORT TITLE

2007/08 SECOND BUDGET REVIEW

REPORT OF

FINANCIAL ADVISER

FOR SUBMISSION TO

DATE

AUTHORITY MEETING

19 SEPTEMBER 2007

1. SUMMARY OF REPORT

This report is the second in the current year of a series of regular reports on the Authority's finances. It concludes that the Authority is currently forecast to have a revenue surplus of £2.024m at 31 March 2008, i.e. an increase of £1.271m compared with the first review. The report, however, draws attention to issues that could impact on this position. The report also looks briefly at some of the issues and potential budget pressures that could add to the Authority's budget and resource requirements for 2008/09. A further review of the 2007/08 budget, together with an up-to-date assessment of the budget and resource requirements for 2008/09, will be reported to the Authority in December.

2. RECOMMENDATIONS

The Authority is requested to:-

- (i) Note the second review of the 2007/08 revenue budget.
- (ii) Note the potential budget pressures that could further impact on the Authority's 2008/09 budget and resource requirements.
- (iii) Note that a third review of the 2007/08 budget will be reported to the Authority meeting in December together with an up-to-date assessment of the budget and resource requirements for 2008/09.

Signed by the Financial Adviser:

Date:

3. **Introduction**

- 3.1 At the Authority meeting in June I advised Members that the Authority was forecast to have a revenue surplus of £0.753m at 31 March 2008. As a result of the second review forecast revenue balances at the year-end are now estimated to increase by a further £1.271m to £2.024m. This report provides details of the main changes and other issues that have arisen since the last meeting.

4. **Second Budget Review**

4.1 **Transport, Disposal and Landfill Tax: (- £0.960m)**

- 4.1.1 During the period April to July 2007 there has been a net reduction of 3.06% in the level of residual waste entering the waste stream over the same period in 2006/07. On this basis, the 2007/08 residual waste stream is estimated to reduce by 23,803 tonnes to 753,225 tonnes (777,028 tonnes in 2006/07).
- 4.1.2 Details of the percentage movement in 2007/08 residual tonnage levels for each borough compared with 2006/07 tonnages may be summarised as follows:-

Table 1	Current Forecast (April to July)
Barnet	- 2.80%
Camden	- 1.13%
Enfield	- 5.11%
Hackney	+ 0.08%
Haringey	- 3.03%
Islington	- 4.27%
Waltham Forest	- 5.81%
Overall Position	- 3.06%

The figures in table 1 indicate that there has been a significant reduction in the amount of residual waste entering the waste stream in the early part of the year. At the time of writing, officers are not aware of any changes to borough collection arrangements that could have impacted on waste flows. The tonnage reduction in this period is therefore most likely to have arisen because of either a reduction in the amount of waste generated by households, or by an increase in the recycling and composting activity by constituent boroughs. Given, however, the early date of this meeting the Authority has yet to receive the comparable borough recycling and composting data that should enable the Authority to establish the scale of the underlying change in the total waste stream (before recycling and composting activity is taken into account). The position is by no means clear. However, by the time of the next meeting in December the Authority should have received details of actual borough recycling and composting data for the first six months of the year, as well

as an up-to-date full year forecast of these activities. This will help the Authority to form a better understanding of the waste stream activity in the north London area.

- 4.1.3 Based upon information available at the time of determining the 2007/08 budget and levy the transport and disposal budget allowed, on the one hand, for a general 1% growth in the total waste stream and the full year effect of new/re-opening civic amenity facilities (a total increase of 11,760 tonnes), and on the other, a reduction of 16,027 tonnes to reflect the boroughs' planned increase in recycling and composting during 2007/08. As a consequence the 2007/08 transport and disposal budget was based upon a residual waste stream of 771,700 tonnes. Assuming the current forecast of 753,225 tonnes remains valid this would result in a reduction of 18,475 tonnes and transport and disposal saving of £0.517m and a landfill tax saving of £0.443m, i.e. a total of £0.960m.
- 4.1.4 The Authority's waste contracts are linked to changes in the Retail Price Index (RPI). The 2007/08 budget allows for an increase of 3% at the relevant review date for these contracts. At the time of writing, the RPI data available for the year to July 2007 indicates that the annual rate of increase is 3.8%, i.e. a one per cent reduction compared with the recent high of 4.8% reached in May 2007. This is particularly significant as most of the Authority's contracts are linked to a December/January price review. Whilst there is still time for the growth in inflation rates to retreat further over the coming months there remains a risk that the current budget assumption of 3% could be tested. No adjustment is made in the current budget review for the potential effect of a higher inflation rate but this will need to be reviewed further at the next meeting.

4.2 **Recycling Credits and BMW Diversion Incentive Scheme**

- 4.2.1 The 2007/08 budget continues to allow for the payment of recycling credits to boroughs that take waste out of the waste stream by virtue of their recycling or composting activities (although the Authority's duty to pay recycling credits ceased on 1st April 2006, the Authority has previously decided to operate a local recycling credit scheme to coincide with the phasing-in of the new default arrangements for apportioning the levy), and an incentive scheme to reward boroughs that take biodegradable waste out of the waste stream. With reference to the discussion at paragraph 4.1.2 above, the 2007/08 budget assumptions could be tested if data received from the boroughs reveals that the reduction in the waste stream has been caused by a higher than assumed level of borough recycling and composting activity.

4.3 **Non-household Charges: (+ £0.416m)**

- 4.3.1 Under the Authority's current arrangement for calculating non-household tonnages/charges the reduction in the residual waste stream (paragraph 4.1.1) will also have a direct impact on the Authority's non-household income. Compared with an original budget assumption of 155,956 tonnes the current forecast assumes that non-household tonnages will reduce to 148,645 tonnes, i.e. a reduction of 7,311 tonnes and a reduced income of £0.416m. The non-household charging arrangement is currently under review and subject of a report elsewhere on this agenda, however, any changes will not be applied to the current year.

4.4 Contribution to Earmarked Reserve (Recycling): (- 0.386m)

4.4.1 At its meeting on 27 June the Authority decided to cease making annual contributions to its earmarked recycling reserve. Members will recall that the reserve was originally established following the receipt of a special dividend payment of £1m from LondonWaste Ltd in 2000/01, and that the reserve had been supplemented each year since then by a sum equivalent to the notional interest on the balances held in the reserve. Although Members wished to retain the original provision of £1m to assist with the funding of its future treatment facility needs, the meeting also decided that the cumulative contributions of £0.320m that had been made to the reserve in the seven-year period to 31 March 2007 should be returned to the Authority's general balances and that no further contributions should be made. The combined effect of these changes will return £0.386m to general balances in 2007/08.

4.5 Recycling Credits and Other Recycling Initiatives: (- £0.195m)

4.5.1 The 2007/08 approved budget includes a provision for payments to third parties under the re-use and recycling credit scheme. As the Authority subsequently decided not to support the registration of two profit-making companies this will release a budget provision of £0.167m.

4.5.2 Elsewhere on this agenda a report reviewing the support programme for 'real nappies' indicates that the expansion of the nappies project has been slower than envisaged and that not all boroughs have signed-up to Real Nappies for London Scheme (RNfL). As a result it is envisaged that there will be a budget saving of at least £0.028m.

4.6 WEEE Directive: (- £0.077m)

4.6.1 The 2007/08 budget reflects the change to producer responsibility from 1st July 2007 for the take back of electrical appliances under the Waste Electrical and Electronic Equipment Directive. Although it was necessary for the Authority to budget for the full cost of treatment and disposal in the first quarter it was envisaged that the Authority would only incur a handling charge thereafter. The Authority has been successful in negotiating a lower than budgeted price which should result in a budget saving of £0.077m.

4.7 Summary

4.7.1 Table 2 provides a summary of the 2007/08 financial position:-

Table 2

	2007/08 Original Budget	2007/08 First Review	2007/08 Second Review	Variance between 1st & 2nd Review
Expenditure	£'000	£'000	£'000	£'000
Main Waste Disposal Contract (Ex CA Waste)	26,774	26,774	26,257	(517)
- Clinical Waste	269	269	269	
- Fridges and Freezers	218	218	161	(57)
- In-Vessel Composting Facility	1,697	1,697	1,697	
- Dry Recyclable Bulking Arrangement	1,256	1,256	1,256	
Civic Amenity Waste	1,659	1,659	1,659	
Landfill Tax	7,073	7,073	6,630	(443)
Hazardous Waste – TV and Computer Screens	82	82	62	(20)
Hendon Transfer Station	447	355	355	
Hornsey Street Transfer Station	2,982	2,911	2,842	(69)
Recycling Credits	3,477	3,477	3,310	(167)
Other Recycling Initiatives	129	141	113	(28)
BMW Diversion Incentive Scheme	642	642	642	
Agency Services	514	574	574	
Waste Strategy and Contracts Group	896	896	896	
Waste Contract – Procurement Costs	700	700	700	
Annual Compensation	33	33	33	
Provision for Possible Litigation Costs	50	50	50	
LATS – Use of Allowances	5,875	5,229	5,229	
LATS – Transfer to reserve (surplus allowances)	808	719	719	
Contribution to Earmarked Reserve (Recycling)	<u>66</u>	<u>66</u>	<u>(320)</u>	<u>(386)</u>
	55,647	54,821	53,134	(1,687)
Less				
Income				
Rents	(83)	(83)	(83)	
Interest on Balances	(788)	(1,138)	(1,138)	
LATS Grant	(6,683)	(5,948)	(5,948)	
Estimated Dividend Stream	<u>0</u>	<u>0</u>	<u>0</u>	
	(7,554)	(7,169)	(7,169)	
Net Expenditure	48,093	47,652	45,965	(1,687)
Contingency	<u>500</u>	<u>500</u>	<u>500</u>	
Total Net Expenditure 2007/08	48,593	48,152	46,465	(1,687)
Financed By :-				
Balances b/fwd	(4,808)	(5,120)	(5,120)	
Charges to Boroughs (Non-household waste)	(8,884)	(8,884)	(8,468)	416
2007/08 Levy	(34,901)	(34,901)	(34,901)	
Total Resources Available	(48,593)	(48,905)	(48,489)	(1,271)
Estimated Revenue Balances as at 31 March 2008 (Surplus)	0	(753)	(2,024)	(1,271)

5. **Review of the Outlook for 2008/09, 2009/10 and 2010/11 - Update**

5.1 In June Members were provided with a brief update on the medium term outlook for 2008/09, 2009/10 and 2010/11. This indicated that the cost to constituent councils could rise by up to 14.3% in 2008/09, a further 11.5% in 2009/10 and by a further 7.8% in 2010/11. The main reasons for this were:

- (i) In 2008/09, the need to replace the use of balances used to fund the 2007/08 budget as offset by the fallout of the local recycling credit scheme for the NLWA constituent boroughs;
- (ii) The impact of the landfill tax escalator across all years; and,
- (iii) The cost of the Procurement Process, also across all years.

5.2 **Recycling and Composting Treatment Facilities**

5.2.1 The June report also reminded the Authority that although some allowance had been made for a year-on-year growth in the use of recycling and composting treatment facilities of 20,000 tonnes per annum over this period (55,500 tonnes in 2007/08), the medium term forecasts made no allowance for the very substantial additional costs of implementing the North London Joint Waste Strategy (NLJWS). Although the Authority will require additional facilities before the replacement of its current main waste disposal contract in 2014, preliminary work undertaken in developing a procurement strategy suggested that waste management costs will not begin to rise steeply until about 2013/14 onwards, i.e. outside the scope of this review. Nevertheless, the report further indicated that it would be necessary to examine the growing financial impact of procuring additional treatment facilities, and, or, merchant capacity to meet borough expectations in accordance with the NLJWS. With this in mind boroughs had been asked to provide the Authority with an up-to-date assessment of the potential additional treatment facility requirements that will arise from the transfer of their recycling and composting arrangements to the Authority over the review period.

5.2.2 At the time of writing, based upon the returns received from four boroughs, it is now clear that the boroughs are seeking to arrange for more of their waste treatment needs to be channelled through the Authority at an accelerated rate. The full picture has yet to emerge, and this will be reported to the next meeting of the Authority, however in the case of 2008/09 four boroughs are seeking additional treatment capacity of 42,800 tonnes comprising; 17,000 tonnes of green/kitchen wastes and 25,800 tonnes of co-mingled dry recyclate, i.e. an extra 22,800 tonnes over the additional allowance currently included in the forecast for 2008/09. This could add c. £1.2m to the Authority's budget in 2008/09 and could be greater once all boroughs have informed the Authority of their requirements. However, if the reduction in the 2007/08 residual waste stream continues at current projected levels (paragraph 4.1.3 above), it is possible that the cost of the extra additional treatment capacity may be largely offset by the cost saving arising from a reduction in the waste stream (the projected 2007/08 saving from the waste stream reduction of £0.960m is estimated to be in the order of £1.123m expressed at estimated 2008/09 prices).

5.2.3 Members should also bear in mind that if boroughs transfer more of their current recycling and composting arrangements to the Authority that the additional costs that each council will bear from the increase in the levy in the year of transfer is likely to be significantly more than offset by the direct saving that transferring boroughs will gain when they cease to pay their own third party recyclers for treatment services. This is because, although the Authority will bear the additional cost of treatment in the year it arises, and all constituent councils to varying degrees will share this cost, individual councils will not bear a more appropriate share of the increased levy costs until, in the case of 2008/09, the 2008/09 household waste tonnages are used to apportion the 2010/11 levy under the default arrangements for apportioning the levy. Assuming constituent councils do not agree an alternative basis for apportioning the 2008/09 levy, the household waste element of the NLWA levy will be apportioned in proportion to each council's 2006/07 actual household waste tonnages. Clearly, it is possible for the NLWA constituent councils to agree an alternative levy apportionment basis, however, as this has not happened over the past 21 years it is felt that the most likely outcome is as stated.

5.3 **Capital Programme – Financing Costs**

5.3.1 Following the transfer of waste operations to LondonWaste Ltd in December 1994 it has not been necessary for the Authority to have a capital programme, however, as the Authority begins to prepare for the replacement of its current contract in 2014 and additional new facilities required to meet the requirements of the Landfill Directive the Authority will need to consider how best to finance its facility needs.

5.3.2 The report to the Authority in December 2006 that led to the approval of the Authority's Procurement Strategy concluded that it should be financially advantageous to the Authority to acquire and then offer sites to contractors for their redevelopment and operation (thereby avoiding the higher interest rates that the contractor would incur, and providing greater certainty to successful project outcome). DEFRA, the sponsoring Government department for waste PFI projects has also indicated that an award of Government financial support through the PFI mechanism is likely only where an authority has secured sites for its future facilities. Whilst it is not the intention of this report to pre-empt the findings of the report that will be submitted to the February meeting of the Authority about its proposed PFI submission and the funding options for its facility needs in general, Members are advised that the full year effect of every £1m of capital investment using public sector borrowing could add c. £0.086m to the Authority's budget and resource requirements. Thus, a £10m land acquisition could add £0.860m in a full year, and £4.3m for a £50m site. If the Authority was minded to support a proposal to acquire sites, this could further add to the Authority's budget and resource requirements in the year ahead.

5.4 An up-to-date and detailed assessment of the 2008/09 budget and resource requirements will be reported to the December Authority meeting.

6. **Conclusion**

6.1 Although the second review indicates that there could be an improvement in forecast balances at 31 March 2008 there are a number of uncertainties and potential budget

pressures that could impact on this position. Whilst I am confident that the Authority's overall budget should remain sufficiently robust to meet the cost of its waste disposal obligations in 2007/08, there are a growing number of budget pressures that could impact on the Authority's 2008/09 budget and resource requirements. These will be examined in more detail in December.

7. **Comments of the Legal Adviser**

- 7.1 The Legal Adviser has been consulted in the preparation of this report and has no comments to add.

Local Government Act 1972 - Section 100 as amended

Documents used in the preparation of this report:-
Reports to the Authority 7 February 2007 and 27 June 2007
2007/08 Budgetary Control Working Papers

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