

NORTH LONDON WASTE AUTHORITY

REPORT TITLE:

DRAFT PROCUREMENT STRATEGY

REPORT OF:

HEAD OF WASTE STRATEGY AND CONTRACTS

FOR SUBMISSION TO:

AUTHORITY MEETING

DATE:

20th December 2006

SUMMARY OF REPORT:

This report puts forward the draft Procurement Strategy produced by the Authority's appointed consultants in consultation with the Authority's officers and highlights the key conclusions and recommendations for approval to allow the Authority to proceed with procuring its next waste management contract(s). It also outlines how the consultants arrived at their conclusions and includes timescales for commencing the process.

RECOMMENDATIONS

The Authority is recommended to:

- i) Approve the procurement approach set out in Sections 6, 7 and 8 of this report;
- ii) Make budget provision of £500,000 in the 2007/8 financial year for the engagement of procurement consultants to assist the Authority through its procurement process;
- iii) Engage land agents through the Authority's Valuation Adviser to undertake a site survey of potential additional sites that the Authority might secure to support the large number of new facilities required in the area;
- iv) To develop and draw up draft Inter-Authority Agreements with the constituent Boroughs as set out in Section 10 of this report;
- v) Note that a review of the Authority's governance structure and internal team is being undertaken in the light of the anticipated demands of the procurement process;
- vi) Make a further budget provision of £200,000 for staffing in the 2007/8 financial year for the additional resources required to manage the procurement of the new contract(s).

**Signed by Head of Waste Strategy
and Contracts**

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Date:.....

1.0 PURPOSE OF THE REPORT

- 1.1 This report puts forward the draft Procurement Strategy produced by the Authority's appointed consultants in consultation with the Authority's officers and highlights the key conclusions and recommendations for approval to allow the Authority to proceed with procuring its next waste management contract(s). It also outlines how the consultants arrived at their conclusions and includes timescales for commencing the process.

2.0 BACKGROUND

- 2.1 The North London Joint Waste Strategy (NLJWS) identified the actions the Authority would need to take to achieve the recycling and composting targets set out within it and in order to meet its obligations under the Landfill Allowance Trading scheme. The NLJWS set out a list of new facilities for the recycling, composting and treatment of residual waste that would be required from 2004 in order to achieve its objectives (see Appendix 1). In addition to this, the Authority's Main Waste Disposal Contract with LondonWaste Limited (LWL) for the energy-from-waste incineration of residual waste and (by variation), certain other waste treatments, is due to expire in December 2014. The Authority is required to procure a new contract(s) and ensure that this achieves the objectives of the NLJWS. As shown in Appendix 1, some of the new facilities are required before the end of the current contract.
- 2.2 In order to provide such a wide range of new facilities and associated services alongside procuring a new waste management contract(s), the Authority engaged consultants to provide expert advice from legal, financial and technical perspectives. A report to the April 2006 meeting of this Authority detailed the consultants that had been engaged to provide these advisory services. The successful consultants were KPMG for financial advice and also lead consultant, Eversheds for legal advice and Entec for technical advice.
- 2.3 The consultants were required to undertake a series of legal, financial and technical modelling exercises from their expert knowledge, drawing upon other procurement experience underway in other waste disposal authorities around the country, to assist the Authority to decide its approach towards future facility and service procurement. A thorough and rigorous assessment of the local complexities and the development of potential commercial solutions through financial, legal and additional technical analysis and preliminary market testing was carried out to achieve this.

- 2.4 The consultants' work has culminated in the production of a draft Procurement Strategy that includes key conclusions and recommendations to the Authority that is now presented to this Authority for approval. The complete document with appendices is available on request.

3. CONSULTANTS' PROGRESS

- 3.1 The consultants' work has built upon and progressed the identified waste growth and corresponding facility needs identified in the NLJWS and a significant amount of time and effort has been focussed on the following areas:-

- Identifying the legal issues involved including identifying the relevant procurement laws applicable (Section 5 of the draft Procurement Strategy)
- Updating waste projections and predicting forward to 2044, beyond the scope of the NLJWS (Appendix 2 of the draft Procurement Strategy)
- Updating waste growth and housing growth forecasts (Appendix 3 of the draft Procurement Strategy)
- Updating the timescales for facility need and types of facility required (Appendix 12 of the draft Procurement Strategy)
- Identifying the opportunities and constraints around the availability of suitable sites for the facilities required (Appendix 1 of the draft Procurement Strategy)
- Identifying a long-list of options for structuring contracts (Appendix 5 of the draft Procurement Strategy)
- Short-listing of the contract structure options (Appendix 9 of the draft Procurement Strategy)
- Assessing the market interest and appetite for the Authority's contract(s) and ensuring competition (Section 11 of the draft Procurement Strategy)
- Identifying and analysing the risk share allocations of contract structures (Section 12 of the draft Procurement Strategy)
- Identifying the funding routes available including the suitability of PFI (Appendix 4 of the draft Procurement Strategy)
- Providing estimates of the potential facility capital and operating costs (Appendix 8 of the draft Procurement Strategy)
- Producing costings models for affordability purposes (Section 13 of the draft Procurement Strategy)

- 3.2 The full report of this work is available on request.

4.0 STRATEGIC ASSUMPTIONS

4.1 Due to the complex nature of the range of issues being considered, it was necessary to carry out the modelling of options under a set of strategic assumptions. The key assumptions are listed below and were developed from the NLJWS assumptions and expanded upon from the consultant's experience in co-operation with the Authority's officers and having regard to other procurements currently being undertaken.

4.1.1 Waste Growth

Waste will grow in line with the NLJWS assumptions of 3% from 2006-2010, 2.5% from 2011-2020 but will reduce to 0.7% from 2021 onwards. The reduced growth rate from 2021 assumes no further growth in waste per household, but does take account of new additional housing in the area producing new waste.

4.1.2 Meeting Targets

The procurement strategy must achieve the recycling and composting targets set out in the NLJWS. In addition, the strategy aims to ensure that the Authority is not ever reliant on purchasing landfill allowances from another waste disposal authority.

4.1.3 Purchasing Position

The Authority's interests as a purchaser of facilities and services for waste treatment and disposal takes precedence over its interests arising from its 50% shareholding interest in LondonWaste Limited (LWL).

4.1.4 Ownership of Land and Facilities

For the purposes of modelling it has been assumed that land for new sites is bought and owned by the Authority and that all treatment facilities are provided by the Authority through contracts.

4.1.5 NLWA / Borough Roles

The Authority and the Boroughs are jointly responsible for waste reduction and reuse measures. The Boroughs are responsible for collecting waste for recycling, composting and residual treatment and delivering it to the Authority, which is responsible for making arrangements for the actual recycling, composting and treatment of that waste.

4.1.6 Technology

No decisions have been made regarding the use of specific recycling, composting and waste treatment technologies. The modelling has used prices known by the consultants from their work relating to the procurement of similar facilities elsewhere for the purposes of producing preliminary costings.

- 4.2 A full list of the assumptions that were made to carry out the modelling exercise is listed in Section 7 of the draft Procurement Strategy. From these assumptions, the consultants produced a 'Reference Project', which is the full list of facilities the Authority needs to provide to achieve its targets, with costings of this list set out over the lifetime of the expected contract period (ie 30 years from 2014). It is important to note that the 'Reference Project' is a starting point for the Authority to gain some preliminary costings for affordability purposes and to provide some important information for the Authority to begin procurement. It may not represent the final range and number of facilities that will eventually be provided as this will be heavily dependant on the outcomes of the procurement exercise and the availability of sites.

5.0 KEY ISSUES IDENTIFIED

- 5.1 A number of key issues that could affect the Authority's procurement process have been identified during this project, in particular, the Authority's ability to attract genuinely competitive bids from a range of companies in the marketplace. In order to get an early idea of market interest and opinion on contract structures, a soft market testing exercise was carried out in July, during which over 100 waste service and technology providers and funders were invited to comment on the proposed structures, along with SITA our joint venture partner.
- 5.2 The results of the exercise generally revealed that the larger waste companies would prefer to work with the Authority through an integrated contract, taking responsibility for co-ordinating the various technology providers and waste flows between facilities and operations, whereas the smaller technology providers would prefer to contract directly with the Authority and operate their own facilities. The outcomes of the soft market testing exercise are contained in Section 11 of the Draft Procurement Strategy.
- 5.3 A key risk that has been identified from this process is the potential pre-conception from the waste industry that the Authority's joint venture partner would have a significant advantage in any future procurement of any waste contract(s), mainly due to the nature and length of the joint venture partnership and the ownership of the Edmonton site by LondonWaste Ltd. The Authority's procurement team has been strongly advised by the consultants that any further development of facilities at the EcoPark through the main waste disposal contract, should ensure that all reasonable steps have been taken to maintain the Authority's ability to secure best value in subsequent larger procurements.

- 5.4 A further key issue that was brought out during the soft market testing exercise is the level of commitment from the constituent Boroughs to the Authority's procurement process. The waste industry mentioned concern that there had been a delay to adoption of the NLJWS and sought confirmation that the Boroughs will be fully signed up to the procurement process before the tendering process begins. This is essential to provide certainty to waste companies in the process and will determine whether the Authority attracts sufficient bids of a high quality. The costs involved in tendering to companies can be £2-3 million for large complex contracts and senior staff are engaged for lengthy periods of time, so it is necessary for it to be worth their while bidding. Section 10 of this report puts forward a form of agreement between the Boroughs and the NLWA to provide this commitment.
- 5.5 Other key issues that may limit the number of companies interested in the Authority's procurement include the capacity and ability of the waste industry to respond to the large volume of contracts currently being prepared for and tendered by waste disposal authorities in the UK. This too may have a bearing on the outcome of the procurement process and whether the Authority decides to tender facilities and services individually or in groups of services.

6.0 DRAFT PROCUREMENT STRATEGY – CONSULTANTS' KEY CONCLUSIONS

- 6.1 The Authority's procurement consultants have set out a number of conclusions to assist the Authority begin its procurement work, contained within the draft Procurement Strategy. The key conclusions are summarised below:
- 6.2 The Authority has a duty to procure a new waste management contract(s) and continuing with the current levels of recycling, composting and waste recovery ie the 'business as usual' model is not a viable option for the Authority. In addition to this, there is no provision within the existing contract with LWL for any extensions to that contract.
- 6.3 The Authority has short-term (before the end of the contract in 2014) and long-term procurement needs which adds a layer of complexity to the process. The short-term facility provision must have regard to the long-term needs of the Authority.

- 6.4 The long-term procurement needs of the Authority involve the provision of multiple facilities that have long lead times within the planning, construction and commissioning stages. As such, this procurement needs to start as soon as possible.
- 6.5 The total procurement requirements of the Authority to meet the NLJWS and LATS targets will involve significant costs that the constituent Boroughs will need to fund through the levy or other payment mechanism.
- 6.6 The Authority will be procuring in a climate whereby many other waste disposal authorities are procuring to achieve 2010 LATS targets. The NLWA will have the added local pressure of competing for construction services due to the 2012 Olympics works.
- 6.7 The NLWA needs to take steps to increase market interest in its procurement to mitigate the risks mentioned in 6.1.5 and also the NLWA needs to package its contract(s) to maximise active market competition to provide local services.
- 6.8 The current waste management sites used and/or owned by the NLWA are not sufficient for its future facility requirements. Additional sites need to be provided.
- 6.9 The consultants' analysis of potential contract structures does not show significant differences in terms of risk and cost over the lifetime of the contract(s). A preferred contract structure is therefore not necessarily conclusive, although a joint venture partnership approach between the public and private sector appears to offer advantages.
- 6.10 Significant differences in cost are likely to come from the type of funding chosen by the Authority over the lifetime of the contract(s).
- 6.11 The use of PFI credits to supplement the costs involved in an integrated waste management contract or for a residual treatment contract only, may not be sufficient to attract the Authority to this funding route due to the size and scale of this procurement.
- 6.12 The constituent Boroughs commitment to the procurement process is a significant risk that could affect the outcome of the process. This needs to be given more certainty through strengthening the relationship between the Authority and the Boroughs.

7.0 DRAFT PROCUREMENT STRATEGY – CONSULTANTS’ KEY RECOMMENDATIONS

- 7.1 The draft Procurement Strategy sets out a number of recommendations contained in the Executive Summary and Section 2 of the full document. The key recommendations are listed below:
- 7.2 In order to encourage competition, the consultants have recommended that the Authority will need to give careful consideration to the packaging of its future waste management services to ensure flexibility and in order not to rule out an optimal solution that may emerge.
- 7.3 The procurement of the long-term replacement to the current main waste disposal contract must start as early as possible in 2007 in order to ensure that contract(s) can be signed by the end of 2009. This then allows five years for the planning, construction and commissioning of facilities to be carried out.
- 7.4 The provision of facilities for the short-term procurement needs should be decided on a facility-by-facility basis having regard to the long-term procurement process.
- 7.5 The Authority needs to undertake a site survey of the potential for securing additional sites to support the large number of new facilities required in the area. This survey should be carried out as soon as possible to enable the Authority to enter procurement in 2007 with a site to offer to the market.
- 7.6 The Authority should agree to use the new Competitive Dialogue procurement route to optimise contract packaging and contract structures on the basis of tenders received. The Competitive Dialogue process is encouraged for particularly complex contracts and is therefore appropriate for replacing the existing waste management contract.
- 7.7 The Authority should consider the use of prudential borrowing through the Public Works and Loans Board to reduce the long-term interest payments on capital spend. It should also use the Competitive Dialogue process to run ‘funding competitions’ to optimise funding options for specific project costs.
- 7.8 The Authority needs to review its in-house organisation to ensure it is sufficiently resourced to meet the demands of the procurement process and the subsequent contract management activity.

8.0 RECOMMENDED PROCUREMENT APPROACH

- 8.1 As set out in Sections 6 and 7 of this report, the consultants work has culminated in a number of key conclusions and recommendations to the Authority. Through these, a recommended procurement approach has emerged, the key components of which concern how to commence the procurement process and considerations for financing the major capital investment required.
- 8.2 It is recommended that the Authority use the Competitive Dialogue route to begin the procurement, which will enable bidders to put forward contract structuring solutions as part of their bid elements. This will allow flexibility to the Authority to structure the contract in the way suggested in paragraph 7.2 of this report if satisfactory integrated solutions are not forthcoming or are not the best available option.
- 8.3 With regard to financing the large capital investment required, it is recommended that the Authority uses prudential borrowing through the Public Works and Loans Board (PWLB) to secure the land required for new facilities and that this funding is also considered to fund the less capital intensive and less technologically complex facilities such as the Materials Recovery Facilities and In-Vessel Composting Plants. Whilst the financial modelling by our consultants suggests that public sector borrowing is likely to be the most cost effective solution, it is not necessary to fix the Authority's funding strategy at this time. It is recommended that this is determined during the bidding process by using 'funding competitions' to attract private sector funding, using the PWLB interest rate levels as a benchmark.

9.0 MANAGING THE PROCUREMENT PROCESS

- 9.1 The procurement process is estimated to take approximately two years from the placing of the OJEU notice to the signing of contracts, during which time the Authority's procurement team and Advisers will be actively engaged in the process. Following this there will be significant activity within the team to deliver the outcomes of the procurement. The advice of the Authority's consultants is that the current internal resources and governance structure are not sufficient to manage the high volumes of work expected. Further use of external consultants will be required throughout the procurement process. It is proposed to make an estimated budget provision of £500,000 in the 2007/8 financial year.

- 9.2 As part of the consultant's work, a survey of other waste disposal authorities with similar procurement needs was carried out, to provide information on the levels of resourcing these authorities have to manage their procurement processes. Appendix 2 of this report summarises the procurement team structures and contract sizes of three of the larger waste disposal authorities currently in procurement, for comparison with the NLWA's current resourcing structure.
- 9.3 Appendix 2 shows that the NLWA currently has a significantly smaller team than other comparable waste disposal authorities engaged on large scale procurement projects. In the light of this, the Authority is currently reviewing its internal team and governance structure to ensure it has the ability to manage the levels of work expected. It is proposed to make an estimated budget provision of a further £200,000 in the 2007/8 financial year for the additional staff of different levels of seniority and skills that will inevitably be needed to manage this highly complex and significant programme of work. Specific proposals will be brought to Members as soon as possible.

10.0 BOROUGH IMPLICATIONS

- 10.1 Section 5 of this report highlights the importance of commitment from the constituent Boroughs to enable the Authority to attract sufficient competition to its joint procurement project. Experience from other waste disposal authorities has shown that enhanced levels of agreement or 'Inter-Authority Agreements' between the WDA and the constituent Boroughs have proven to be essential to provide a level of confidence in the waste and financial marketplace. They are also required by DEFRA as part of any application for PFI credits.
- 10.2 The NLWA needs to demonstrate commitment from the Boroughs to a partnership approach for the procurement process. In particular the Authority needs to have certainty from the Boroughs in key service areas to provide a level of confidence to the waste industry that the NLWA can deliver its procurement project. These key areas include:
- Agreeing waste flows and service specifications;
 - Committing to operating collections of recyclables and compostables from households;
 - Providing the recyclable and compostable material to the NLWA for treatment;
 - Informing the Authority in a timely manner of any changes to collection services;
 - To provide an effective planning framework for new waste facilities through the Joint Waste Development Plan Document;

- Involvement in Authority steering groups during the procurement process;
 - Funding new facilities through the levy.
- 10.3 The Authority is working up a draft 'Inter-Authority Agreement' that will confirm Borough commitment to the Authority's joint procurement process and confirm commitment to provide the recyclables to the Authority. It is likely to set out some form of material specifications and payment mechanisms between the Authority and the Boroughs. A draft agreement will be prepared in line with the principles of the NLJWS and the partnership approach agreed. Any issues in principle will be brought to Members for agreement.
- 10.4 In order to engage with Boroughs throughout this process and highlight issues of interest to them, the Authority's officers have carried out a series of group meetings, presentations and one-to-one meetings with Technical Officers, Directors of Environment, Directors of Finance, Executive Members for Environment and NLWA Authority Members. This process has served to highlight emerging issues for the Boroughs particularly in relation to future Authority funding issues and recycling collection services.

11.0 FINANCIAL IMPLICATIONS

- 11.1 The draft procurement strategy seeks to deal with both the implementation of the North London Joint Waste Strategy (NLJWS) and the need to secure a new waste management contract(s) to replace the current contract with LondonWaste Ltd which is due to expire in December 2014. Underlying this is the Landfill Allowance Trading Scheme (LATS), which is a powerful financial driver to ensure that the Authority remains LATS compliant. Failure to do so could expose the Authority to fines of £150 for every tonne of waste sent to landfill above the Authority's annual allocation.
- 11.2 Against the background of a rising waste stream and a reducing number of Landfill Allowances the Authority's consultants have modelled the financial impact of procuring, operating and maintaining a wide range of possible facilities that should enable the Authority to remain LATS compliant in the period to 2044/45. As most of the major new facilities are needed to be operational by 2015/16 there is likely to be a significant stepped change in the Authority's revenue budget requirements in the period between 2013/14 and 2015/16.

- 11.3 Compared with the Authority's current treatment and disposal costs of £47m (2006/07) the consultants have estimated that the Authority's costs could rise in real terms to between £88m (87%) and £96m (104%) by 2015/06, and to between £113m (139%) and £124m (193%) by 2044/45, depending upon the financing solution. All costs are shown at current prices. The lower figure of each range assumes the use of public sector borrowing for both land acquisition and the initial cost of providing the new facilities, whereas the higher figure assumes that private finance has been used in the main to fund the initial cost of new residual waste facilities. Although at this early stage the private finance option appears to be the more expensive funding solution, the financial modelling currently assumes a low level of Government funding support through the Private Finance Initiative relative to the costs of the whole procurement programme. This could change if the Government were to direct more funds to the waste PFI initiative. The Authority will therefore need to establish as a matter of some urgency whether or not this is likely.
- 11.4 Although the costs of implementing the joint waste strategy will have a major impact on the costs of the Authority, and as a consequence the constituent boroughs, the cost of not taking action is estimated to be significantly greater, i.e. costs could rise to £178m at current prices by 2044/45. This scenario assumes that the Authority would incur substantial penalties under the Landfill Allowance Trading Scheme. This can be seen graphically at Appendix 3.
- 11.5 Over the coming year it is envisaged that the Authority will begin to incur significant costs both in terms of the use of consultants and the need to strengthen the internal support arrangements of the Authority. The 2007/08 budget forecast allows for a budget provision of £0.500m for the first, and £0.200m for the second. These are estimated costs and it is envisaged that a similar, if not higher, level of budget provision will almost certainly be required in 2008/09 and 2009/10. Work over the coming year will also help crystallise the scale and timing of the Authority's capital investment needs.
- 11.6 In relation to 2006/07, the Authority originally approved a budget provision of £0.500m. Allowing for the work undertaken to date and the cost of taking the Strategy forward during the remainder of the year a budget provision of £0.250m should now be sufficient. This reduction has been allowed in the 2006/07 third budget review reported elsewhere on this agenda.

12.0 LEGAL IMPLICATIONS

- 12.1 The Legal Adviser should advise at each stage of the procurement of any new waste management contract to ensure that the Authority complies with its own Contract Standing Orders, Best Value principles and the EU Public Procurement Regime. In view of the scale and complexity of this procurement, specialist external legal advice will also need to be sought by the Authority.
- 12.2 The Authority commissioned advice from leading counsel in 2003 as to whether the existing waste disposal contract due to expire in 2014 could be extended under EU Law and the advice received was that it could not. Further Counsel's opinion was obtained in 2006 to see whether there was any scope to extend the existing contract under a limited exemption contained within the new Public Contracts Regulations 2006. The advice received indicated that it would be extremely difficult to gather the required evidence to rely on this exemption and therefore the Authority is likely to be required to follow a competitive tendering process in letting the new contract to comply with EU Procurement Rules.
- 12.3 Members of the Authority have been previously advised that there may be certain points at which the personal interest of the Authority's A Directors and Substitute Director on the board of LWL becomes prejudicial. What this means is that those Members would not be able to take part in the discussion of any matter where they have such an interest. A prejudicial interest is one in which a member of the public, with knowledge of the relevant facts would reasonably regard as so significant that it is likely to prejudice the Member's judgement of the public interest.
- 12.4 This report is seeking to approve the Authority's procurement approach and make budget provision for the procurement process. It is the Legal Adviser's view that any decision on this will have a direct impact on LondonWaste Ltd and an indirect impact on SITA (UK), the NLWA's joint venture partner. On the basis that both of these are potential tenderers, it is the advice of the Legal Adviser that at this stage of establishing the procurement strategy those A Directors and the Substitute Director will have a personal and prejudicial interest in the procurement and will need to absent themselves from those discussions. In addition, it is highly likely that after this meeting, any further discussion of this procurement process at Authority meetings will also trigger a prejudicial interest for those A Director Members.

13.0 RECOMMENDATIONS

13.1 This report puts forward a number of recommendations for approval. The Authority is recommended to:

- i) Approve the procurement approach set out in Sections 6, 7 and 8 of this report;
- ii) Make budget provision of £500,000 in the 2007/8 financial year for the engagement of procurement consultants to assist the Authority through its procurement process;
- iii) Engage land agents through the Authority's Valuation Adviser to undertake a site survey of potential additional sites that the Authority might secure to support the large number of new facilities required in the area;
- iv) To develop and draw up draft Inter-Authority Agreements with the constituent Boroughs as set out in Section 10 of this report;
- v) Note that a review of the Authority's governance structure and internal team is being undertaken in the light of the anticipated demands of the procurement process;
- vi) Make a further budget provision of £200,000 for staffing in the 2007/8 financial year for the additional resources required to manage the procurement of the new contract(s).

14.0 Local Government Act 1972 Access to information

14.1 References

NLWA: *'Procurement Strategy – Consultancy Support'* 5th April 2005

NLWA: *'Procurement Options and Tasks Report'* 8th February 2006

NLWA Consultants: *'Draft Procurement Strategy'* November 2006

Contact Officers: Rachel Espinosa, Procurement Manager &
Andrew Lappage, Head of Waste Strategy & Contracts

Unit 169, Block 1B
Lee Valley Technopark, Ashley Road
N17 9LN

Tel: 020 8489 5730

Fax: 020 8365 0254

E-mail: post@nlondon-waste.gov.uk

Report Ends

APPENDIX 1

Facilities Required as set out in the North London Joint Waste Strategy

Facility Type	Date of Implementation	Tonnage Capacity
Materials Recovery Facility #1	2004	100,000
In-vessel Composting Facility #1	2005	75,000
In-vessel Composting Facility #2	2007	50,000
Materials Recovery Facility #2	2009	100,000
Recycling Bulking Facility #1	2009	30,000
In-vessel Composting Facility #3	2010	75,000
Materials Recovery Facility #3	2013	100,000
Energy from Waste Facility (replacement)	2015	450,000
Mechanical Biological Treatment #1	2015	250,000
In-vessel Composting Facility #4	2017	75,000