BUDGET 2016-17
WDA/03/16

Recommendation

That the Authority:

1. approves the revised budget for 2015-16;

2. approves the revenue budget for 2016-17;

3. considers the Levy proposals set out in Appendix 2 to this report and agrees the proposal for a Levy of £66,247,010;

4. authorises the Levy to be made on the constituent District Councils for 2016-17;

5. agrees the payment dates for the levy; and

6. agrees to the proposed capital programme;

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BUDGET 2016-17
WDA/03/16

Joint report of the Chief Executive and the Treasurer

1. Purpose of the Report

1.1 The Authority is required to prepare a budget and to set a Levy each year. The level of Levy to be charged to each of the constituent Local Authorities needs to be agreed annually alongside a Levy payment schedule. The Authority also needs to consider and approve capital programme proposals.

2. Background

2.1 The Authority is statutorily required to manage the disposal of household waste for Merseyside District Councils and provides services on behalf of Halton Council. The Authority delivers this principally through contracts with private sector contractors who provide waste management and disposal facilities.

2.2 For a number of years the key contracts have been the Landfill Contract held by Mersey Waste Holdings Limited (that the Authority has access to) and the Landfill Top-Up Contract which together provide access to landfill for the Authority's residual household waste. The other key contract is the Waste Management and Recycling Contract (WMRC) operated by Veolia ES. The WMRC includes the provision of transfer stations, waste transport, household waste recycling centres; materials recycling facilities, food waste processing, and has the potential for green waste composting. Together these contracts have enabled the Authority to manage the recycling, treatment and disposal of Merseyside and Halton's household waste. In addition the Authority also leads for the Strategic Waste Partnership on waste minimisation and education initiatives, as well as managing historic closed landfill site liabilities.

2.3 In order to reduce the extent to which the Authority has relied on landfill for disposal which incurs landfill tax at £82.60 per tonne, the Authority entered into interim arrangements to divert waste from landfill. One of these is a 'framework contract' which has a three year term and for which the third year has been let (in September 2014). These interim contracts with FCC recycling and Greater Manchester Waste Disposal Authority have successfully diverted waste from landfill while at the same time saving the Authority some £4M over the time that they have been in place.

3. New disposal arrangements

3.1 The Authority signed the Resource Recovery Contract (RRC) in December 2013 which will enable the Authority to move away from disposal by Landfilling. The contract with Sita Sembcorp UK involves the construction of an Energy from Waste plant in Redcar and a Rail Transfer Loading Station in Knowsley. Waste for disposal will be received by the Authority from the constituent District Councils and Halton Council (under an Inter Authority Agreement) and will be transferred by rail from Knowsley to Redcar where it will be used by the contractor to generate electricity.

3.2 The construction of both the facilities, in Redcar and Knowsley is nearing completion and at the time of writing is on schedule (or even a little early). It is currently expected that the Commissioning phase will commence from March 2016 and that the facilities will become fully operational after October 2016. By the end of 2016-17 and during 2017-18 the Authority should be able to minimise landfilling and the new contract should start to deliver environmental benefits for Merseyside and Halton.

3.3 There should, however, be some caution at this point. While the construction phase is, at the time of writing, going to plan (and even slightly ahead of schedule) this is a very significant engineering project and unplanned factors may cause delays over the next 12 months. In addition the lesson from colleagues in Greater Manchester (and via our interim contract) is that commissioning may not always be completed according to schedule and delays may occur. If there are delays there will be a financial impact on the Authority as landfilling will continue for longer than hoped for.

3.4 The early years of the contract will be challenging financially as the opportunities for sharing income from third party sales of treatment facilities and electricity income are limited in the first years of the contract. The Authority's flexibility to manage those costs without an impact on the Levy was limited when the Sinking Fund which became the Waste Development Fund was returned to constituent District Councils. The RRC overall is a good environmental and financial deal for Merseyside and Halton, but the transition from Landfilling to the Contract is a difficult one.

4. External factors

4.1 The general economic climate and the Government's spending reviews have meant that local government generally, and Merseyside in particular, continues to face very significant changes in the levels of funding available. The Government has once again set very challenging financial targets for Councils and although they have responded well to the changes in their financial resources up to now, those challenges mean that very difficult decisions are having to be made about the shape and size of local government services in the future.

4.2 In 2015-16 Merseyside Councils continued to face very significant savings targets, and for 2016-17 and beyond further very significant savings are required. The Councils have so far been able to make the additional savings but this has been through redesigning services and service provision. They are already looking towards 2017-18 and beyond where additional large savings continue to be required.

4.3 The financial climate for the Councils means that the onus on the Authority is to ensure that the Levy agreed does not impose an unnecessary burden on the Council budgets. The Authority, District Council Treasurers and District Council Chief Executives and Leaders have been discussing the Levy and the strategy for both supporting Districts while at the same time enabling this Authority to meet its statutory and fiduciary duties in the most prudent manner.

4.4 The Authority has not increased its Levy on District Councils in overall terms for a period of six years. While this has been possible for a period of time it is increasingly looking more difficult to achieve going forward. In 2014-15 the Authority's Levy was £3m lower than the budgeted expenditure, supported by a contribution from balances. This pattern has continued and grown into the current financial year with a planned £3M from balances and £4M from a contribution from the Authority's wholly owned company, Mersey Waste Holdings Limited; a total of £7M.

4.5 In this context and with additional significant growth from the new Household Waste Recycling Centre at Old Swan in Liverpool, as well as significant additional financial pressure from the transition to the RRC, particularly after the use of interim contracts to artificially keep the cost of disposal below that of landfill, the Authority held discussions with the Chief Executives of the constituent District Councils with a view to increasing the Levy in overall terms by 2%. There was also the potential for further increases in future years.

4.6 The view from the Chief Executives was that the Authority should also model reductions in the Levy, of 2%.

4.7 The pressure from the District Councils is understandable, but is difficult for the Authority to respond to. The vast majority of the Authority's costs are generated from waste arisings, and the costs associated with treating them. Unless the overall amount of waste, both for disposal and recycling reduces by a considerable amount it is difficult for the Authority to reduce the budget and to set a Levy in line with or lower than prior years. At the same time with no levy increase the Authority's financial reserves from all sources will be depleted more quickly than expected, making the financial position of the Authority perilous.

4.8 The views of Members of the Authority about potential savings options have been canvassed by officers via workshop presentations and the Members' Forward Planning Panel meetings. The Chairperson and Deputy Chairperson of the Authority have shared their views on budget proposals both in these forums and separately. Members' views on potential cost reductions have been reflected in the budget proposals for the Authority to consider.

5. The budget

5.1 The revised estimates for 2015-16 have been established from the Authority's projected activities in the year and the projected levels of spending by the Authority; including the effective management of the Authority's contracts and from the current and projected waste tonnages arising. The outcome of the revised estimate exercise is that the projected level of spending for 2015-16 is likely to be £2.322M lower than originally agreed. The majority of this decrease has arisen because the savings from the continuation of the interim contracts could not be anticipated in last year's budget. In addition there was a significant difference between the amount of recycling credits budgeted for and those that are likely to be claimed by Councils in the year. Finally delays in commencing operations at the Old Swan HWRC have meant there are one-off operational savings which are seen as a windfall in 2015-16.

5.2 The overall effect of this is that the planned level of support from the General Fund balance for 2015-16 may be decreased from almost £2.322M and is in fact projected to be a contribution of some £250k. The Authority's revised estimated for 2015-16 still includes a planned contribution from the wholly owned company MWHL of some £4M from funds no longer required by the company. In the context of the Authority's overall budgets this is helpful and leaves the Authority with balances which enable it to plan to further mitigate some of the impacts of cost growth in the budget in the next year, although these amounts can only be used once and even with proposed savings, without levy increases going forward, the Authority's financial position is at risk of being unmanageable.

5.3 The Authority's proposed budget for 2016-17 is presented at a time when the Authority faces significant financial challenges. From March 2016 through to October 2016 the Resource Recovery Contract is planned to enter into its 'Commissioning' phase. Thereafter, if all goes to plan, the contract should become fully operational and the Authority will make payments for waste treatment under the terms of the contract.

5.4 During the Commissioning phase of the project the Authority's costs are capped to a gate fee, which is slightly lower than the fee at the full operational stage. During this phase the Authority does not pick up additional 'pass through' costs that eventually form part of the monthly 'unitary charge' for the contract. However, at the same time the Authority is not contractually able to take a share of any third party income generated by the contractor, from sales of disposal capacity or from sales of electricity.

5.5 Assuming that Commissioning is successful the Authority then enters into the full operation of the contract where it pays a gate fee per tonne of waste treated, as well as fees for the amount of tonnes of residues from the Energy from Waste Plant, for waste which is accepted for the plant but which cannot be treated. In addition the Authority faces the prospect of additional costs arising from pass through payments, including NNDR which it is required to pay under the contract in proportion to the amount of tonnes disposed of as a proportion of the total. This adds up to a unitary charge which places a significant financial burden of the Authority.

5.6 The financial cost of the Unitary Charge is not mitigated to any significant degree in this period by a share of income from the sale of third party capacity as the Authority is expecting to take most of the capacity in the plant in this early period. Forecasts of additional income from the sale of electricity are not significant in this period, as the price of electricity per Megawatt Hour are currently lower that the contractor has assumed for their own base case.

5.7 During this phase of transition to the RRC the Authority faces a peak in its costs as the initial costs come fully on stream. Over the life of the contract as the amount of waste anticipated to be treated from Merseyside and

Halton reduces the prospects of the unitary charge being held at a relatively steady cost, despite inflation, is realistic. In the event that the waste treatment follows the Guaranteed Minimum tonnage then the contractor will also have the opportunity to sell capacity to the third party market, and under the terms of the contract there will be opportunities for income sharing with the Authority, which may become significant. The incentive for the contractor to sell any additional capacity is tied up not just in sales income, but also in the efficient running of the plant, which works best when near to capacity and the electricity sales that can be generated from that, which are needed to achieve the contractor's base case, but once beyond that are useful for the authority as an income sharing arrangement is in place.

5.8 While the medium to longer term of the contract is very likely to be financially very helpful for the Authority, the transition to the new arrangement and the initial operational period is financially difficult. This difficulty cannot be managed through a sinking fund, as that was transferred to a waste development fund and passed back to the constituent councils. As reported in the Budget approved by Members in February 2015 this was done with the understanding at the Authority that there would need to be modest Levy increases thereafter as the transitional fund was no longer in place.

5.9 During 2015-16 the Authority was able to finalise the development of an HWRC in Liverpool. This will have a part year revenue impact in 2015-16, which is likely to add over £300k to the Authority's revenue budget in that year. The full year impact of the new HWRC in 2016-17 is likely to be over £1M.

5.10 As part of the Authority's continuing drive for efficiency, the way the organisation utilises its resources will continue to be reviewed during the next budget cycle. Where there is scope for additional efficiencies or outcomes to be delivered, then a business case will be developed to outline for Members the costs and benefits of any proposal on an 'invest to save' basis. Where there may be benefit to the Authority from a proposed service development, Members will be asked to approve the release of funds where they are necessary to deliver additional efficiency. Normal improvements in services that may be achieved at no additional cost will be implemented as part of the normal business of the Authority.

6. The Levy Mechanism and recycling credits

6.1 The Levy Mechanism is the methodology used to divide the Levy among the constituent District Councils. The way the Levy is divided is statutory and is based on unanimous agreement by the District Councils over the way the Levy should be apportioned (in the absence of an agreement there is a statutory fallback or 'default' mechanism). The current Levy mechanism was agreed in January 2005 and included an element that related to recycling credits.

6.2 The Waste Disposal Authority has continued to provide a system of recycling credits to constituent District Councils at their request, although the mandatory requirement to provide such credits was removed in 2006.The Authority agreed with the Districts that this continued arrangement incentivised Districts to move away from collecting waste for Landfill. In the Authority's budget for 2015-16 the following amounts were provided:

	£
Amount included in Levy via tonnages	**(6,545,926)**
MWDA Expenditure on Recycling Credits	**6,545,926**

6.3 The total amount planned to be spent and the total amount planned to be raised via the tonnage elements of the levy were the same. In effect this has been a circular flow of funds between the Authority and the Waste Collection Authorities.

6.4 The removal of the recycling credit levy has been discussed by District Council Treasurers on a number of occasions over recent years, but there has been no consensus for the removal of the credits. This is a matter that is part of the Levy mechanism so the Authority cannot unilaterally remove the circular collection and payment of the amounts despite the changes brought about in 2014 by the Local Audit and Accountability Act which mean that the financial impediment to the removal of the Recycling Credits has been eliminated and so the proposal could be considered.

6.5 For 2016-17, if recycling credits were to be removed, the headline impact would be to reduce the Levy by £5.742M.

7. Underlying and future costs facing the Authority

7.1 The Authority continues to keep its funding and affordability model under review now that all the new contracts for long term treatment and disposal of waste have been finalised. At the outset of the procurements a funding envelope that set an annual levy increase at 15.4% was agreed with District Council Treasurers. That envelope allowed the Authority to provide for a Sinking Fund and to plan to use the fund over time to offset future very significant rises in the Levy. (For comparison; if the Levy had continued at that level of increase the Authority would currently be seeking funding of over £130M from District Councils – for 2016-17 the Authority's proposed Levy demand will, in fact, continue to be nearer to half that amount).

7.2 In reviewing the model, the Authority was able to reduce the Levy increase to 12% in 2009-10 and then, in 2010-11, it was able to introduce a zero increase in the overall Levy. In 2011-12 the Authority reduced the Levy by almost £3M with the 'maximum of zero' levy for all constituent Districts. In 2012-13 this 'maximum of zero' approach was repeated and the Authority's overall levy reduced by over £2.5M in the face of increasing cost pressures. In 2013-14 the Levy increase was only £132k or just 0.2% while the overall Levy did not increase for 2014-15 because the Levy was cushioned by a £2.96M contribution from the General Fund. In 2015-16 that cushioning continued with a planned £2M contribution from General Fund and a £4M contribution from the Authority's wholly owned company Mersey Waste Holdings Limited (i.e. a total of £6M).

7.3 The WMRC contract continues to minimise costs to the Authority and together with small overall reductions in waste arisings the Authority has been able to manage with lower than expected levels of Levy. The costs of the landfill which has been the most significant challenge over a number of years will largely cease as the Authority's transition to Commissioning and then to full operation of the Resource Recovery Contract (RRC) will present the biggest challenge, both operationally and financially, over the medium term.

7.4 The underlying costs of the Authority have increase by another £3.9M which is due to a combination of factors including the new HWRC at Old Swan in Liverpool, which adds £1M a year, the end of 'interim contracts' which have temporarily held the disposal costs to the Authority down. Thereafter the cost of the transition to the RRC, initially in the Commissioning phase and anticipated full operation from October 2016 means there is an increase in the Authority's costs. These cost increases are partly offset by savings elsewhere as the Authority has continued to review its budgeted expenditure for 2016-17.

7.5 In consultation with Members through workshop presentations and also via the Members Forward Planning Panel, a number of savings proposals have been developed and are included in the budget estimates as a contribution to reducing the Authority's costs and the impact of the Levy for 2016-17. The following table provides an update on how the savings considered have been taken forward in the budget proposals:

Savings proposal	**Estimated savings**	**Status in the budget proposals**
Removal of Recycling Credits to constituent councils.	£5.7M	This has not been included in the budget proposal because as a levy change it requires agreement by consensus to include in our budget proposal, such consensus has not been reached.
Third party textile recycling credit	£48k	The third party textile recycling credit was retained in prior years as it was initially designed to create an incentive for the collection and recycling of textiles for Merseyside. In the last year the Credit Recycling rate was £25 per tonne. Reviewing the amount generated from the sale of textiles collected, at rates of well over £500 per tonne, it is clear that the strength of the incentive is not as

		significant as it may have been in the past. Therefore the withdrawal of this recycling credit payment has been included in the proposed budget for 2016-17 and beyond.
Bidston Visitor Centre	£30k	The Bidston Visitor Centre provides a way for schools and interested groups to find out about re-use and recycling. This opportunity is provided at the Gilmoss MRF and allowing for the cost of transporting visitors to Gilmoss a saving can be achieved from closing a duplicate facitlity, this has been included in the proposed budget.
HWRC service reductions	£316k	The Authority plans to review the provision of HWRC services across Merseyside. This will mean considering whether reductions in services and/or closures are appropriate. Any proposed changes in services will only be carried out after appropriate consultation has been completed and the

		impact of changes are fully understood and planned for.
Apprentices programme	£60k	Although this has been a popular and a successful programme it is not at the core of the Authority’s activities. The programme has supported District Councils in their provision of apprentice training programmes. District Council Chief Officers have made it clear that reductions in the Authority’s costs are a priority and so the whole of the programme has been withdrawn from the proposed budget for 2016-17.
Education and awareness	£25k	The Authority has continued to provide support for education in community activities which are at the top of the statutory waste hierarchy and which have been successful over a number of years. The proposed reduction in the budget – leaving only £25k going forward, will reduce the impact and effectiveness of the schemes but is done in

		response to real financial pressure.
Re-use scheme	£20k	Re-use is almost at the top of the statutory waste hierarchy and as such promotion of the ideas and approaches to re-use remains important. However, a reduction is proposed in response to the real financial pressure, this will leave some £50k available to support re-use in Merseyside.
TOTAL	£500k	Proposals already included in the draft budget

8. Budget options

8.1 Over the last six years the Authority has delivered initially significant Levy reductions and thereafter has maintained a broadly neutral Levy at a time when its cost base has continued to increase. This has been achieved through a combination of slightly reducing waste tonnages, active contract management, re-engineering of service provision and the regular review of management and administration practices and budgets. This reflects the concern at the Authority to minimise the cost of the Levy to District Councils in a very difficult financial period.

8.2 This approach to minimising the cost of the Levy to districts will continue to underpin the Authority's financial planning in the medium term. However, this comes with a large caveat. The gap between the Authority's budgeted net expenditure and the amounts raised from Districts has been growing; in 2014-15 the gap was £3M, in 2015-16 the budgeted gap was £6M. In 2016-17 and beyond as the interim contracts which have kept costs in check cease, and the RRC comes on stream in its most expensive period that gap continues to get larger.

8.3 In 2014-15 and 2015-16 a combination of utilising the Authority's General Fund and contributions from the wholly owned company have been used to support or 'cushion' these 'gaps' . The prospects for 2016-17 and beyond are more difficult, reserves can only be utilised once, and when they are gone there is no more cushion available to support expenditure. In 2016-17 the gap between the Authority's likely expenditure and the current level of the income from the Levy is £9.901M.

8.4 Despite options for savings being included in the proposed budget it is clear that this is a very significant demand on the Authority's remaining General Fund. While that demand may be met from the remaining General Fund in 2016-17 on a one off basis, it does not address the underlying difference between funding and expenditure facing the Authority in 2016-17 and beyond.

8.5 In order to identify options for the future financial viability of the Authority the Chief Executive and the Director of Finance have met the Chief Executives of the constituent District Councils to explain the current and likely medium term position.

8.6 The Chief Executive and Director of Finance explained the short and medium term financial pressures facing the Authority so that the District Council Chief Executives could understand the context of the Authority's services and costs. The proposal presented to the Chief Executives for consideration was that the Levy be increased in overall terms by 2% for 2016-17, and by 3.5% and 4% in subsequent years. This would enable the Authority to bring the Authority's costs and Levy back into balance over a three year period, while utilising all the Authority's financial reserves.

8.7 One of the reasons for this proposed approach being presented was to provide an opportunity for the Authority to work with the constituent District Councils to review potential savings opportunities, both from the Authority's perspective and from the perspective of the Districts in a strategic and equitable way. If those savings opportunities can be identified it may impact on the scale of future proposals for Levy increases to ensure the financial gap is closed.

8.8 In looking at future potential savings opportunities for the Authority it is important to try to ensure that simply withdrawing services currently provided by the Authority does not load additional costs onto one or more of the District Councils. For example, in Southport there is a waste transfer station that serves mostly Southport and therefore residents of Sefton Council. It would be a very simple decision for the Authority to save the costs of providing that transfer station by closing it down, the knock on effect would be that Sefton Council would have to take waste that had formerly gone to Southport to the Knowsley Rail Transfer Loading Station.

The effect of this closure would be to increase Sefton's costs directly as they would then need to employ additional vehicles and crew to make the additional journeys necessary to ensure the waste could be delivered for disposal.

8.9 Each time the savings from services are considered the Authority must take account of the knock on effect on both waste flows, which do not go away, and on any additional direct costs on District Councils, which do not fall in the equitable way that the Levy was designed to.

8.10 One of the outcomes of the meeting with Chief Executives was an agreement in principle that all of the costs of waste, from collection to disposal should be reviewed as a unified whole, so that the maximum possible savings potential could be achieved for Merseyside overall. When this review is undertaken it will be important to recognise the consequent impacts of any proposal before it is implemented otherwise there may be unintended financial consequences.

8.11 It is also important to recognise that changes to public facing services may not be achieved overnight as requirements of consultation and impact assessments must be made.

8.12 At each stage of any proposed service reduction there will be a need to consider the impact on the contractor, and the contractual requirements for compensation, for loss of profit and redundancy costs for example. In the case of the Authority's contracts, for example they cannot simply be terminated without very significant compensation being paid.

8.13 The Chief Executives of the District Councils asked the Authority to model a 2% reduction in the Levy so that there would be a shared understanding of the impact of that on both the Authority and the District Councils. This modelling has been done and options for the budget present a 2% increase, a static overall Levy and a 2% reduction so that the Authority Members can understand the impact of each option.

8.14 In order to understand the impact of the request for modelling by the Chief Executives group, the following tables have been drawn together. The impacts of these Levy options have subsequently been shared with a further meeting of the City Region's Chief Executives' group. The purpose of the tables is to show that it is difficult to consider the Levy over the course of a single year, but that the potential costs and funding position must be considered over a series of years to have a fuller understanding of the financial position the Authority could be in if it took a short term view.

8.15 To ensure all options are considered the Chief Executive and Director of Finance have modelled a number of scenarios, including the one initially proposed to Chief Executives (2%, 3.5% and 4.4% rises over three years, the third year proposal has been reviewed an is now slightly higher than 4% to remain in balance); the impact of the Chief Executives' requested model (minus 2%, leading to 5.1% and 13% increases); a static levy year followed by catch up years (0%, 4% and 9.2% increases); and a further modest increase (1%, 3.25% and 7.7%).

Option Levy Increases: 2%, 3.5%, 4.4%	**Costs and source of funding**	**Proposed budget**		
		2016/17 £M	**2017/18 £M**	**2018/19 £M**
Expenditure		75.5	76.8	78.2
Income				
	Levy + 2%	(66.9)		
	Levy + 3.5%		(69.2)	
	Levy + 4.4%			(72.2)
	General Fund	(8.6)	(7.6)	
	MWHL			(6.0)
Balance		**0**	**0**	**0**

Option Levy Increases: 1%, 3.25%, 7.7%	**Costs and source of funding**	**Proposed budget**		
		2016/17 £M	**2017/18 £M**	**2018/19 £M**
Expenditure		75.5	76.8	78.2
Income				
	Levy + 1%	(66.3)		
	Levy + 3.25%		(68.4)	
	Levy + 7.7%			(73.7)
	General Fund	(9.2)	(7.0)	
	MWHL		(1.4)	(4.5)
Balance		**0**	**0**	**0**

Option Levy Increases: 0%, 4%, 9.2%	**Costs and source of funding**	**Proposed budget**		
		2016/17 £M	**2017/18 £M**	**2018/19 £M**
Expenditure		75.5	76.8	78.2
Income				
	Levy + 0%	(65.6)		
	Levy + 4.0%		(68.2)	
	Levy + 9.2%			(74.5)
	General Fund	(9.9)	(6.3)	
	MWHL		(2.3)	(3.7)
Balance		**0**	**0**	**0**

Option Levy Increases: -2%, 5.1%, 13%	Costs and source of funding	Proposed budget		
		2016/17 £M	2017/18 £M	2018/19 £M
Expenditure		75.5	76.8	78.2
Income				
	Levy Minus 2%	(64.3)		
	Levy + 5.1%		(67.6)	
	Levy + 13%			(76.4)
	General Fund	(11.2)	(5.0)	
	MWHL		(4.2)	(1.8)
Balance		**0**	**0**	**0**

8.16 In the case of the option proposed at the meeting with the Chief Executives of successive rises on 2%, 3.5% and 4% (final Year now revised to 4.4%) there is a prospect that the Authority's financial position will not lead to the need for what came to be known as 'Cliff Face' increases and with the additional time available to review the way waste is dealt with both at collection and disposal it is likely that some of the costs may be likely to be ameliorated.

8.17 In the case of the option that the Chief Executive's requested the Authority examine, a financial crisis would very quickly develop, after year 1 of the forward budget. The following years' funding gaps would need to be met through Levy increases of 5.1%, followed by a 13% increase the next year to close the remaining gap.

8.18 If the Levy were requested to remain static for 2016-17 then the increases in subsequent years would need to be 4% and 9.2% respectively to get the Authority back into balance.

8.19 The Authority is now proposing that for 2016-17 there should be a Levy increase, in overall terms. The proposal is that the Levy be increased by 1%, which would mean subsequent increases in 2017-18 of 3.25% and potentially in 2018-19 an increase of 7.7%. This proposal provides a financial opportunity for the Authority to work with its stakeholders and partners to identify whether there is scope for any substantive savings to be made through a strategic review of its assets and services, along with any potential further cost savings for Districts from the wider strategic review of the Merseyside municipal waste economy. This will also enable the Authority to fully understand the impact of the Resource Recovery Contract and how it might be utilised to provide the best returns for Merseyside.

8.20 In each case there may be scope for some additional savings to be identified, but that does not address the underlying issue, that by far the largest part of the Authority's costs come from the amount of waste generated, which is outside the Authority's control. Significant savings are unlikely to be achievable without a very significant drop in the amount of waste delivered for treatment. Simply withdrawing services is unlikely to have the required effect as in most cases the waste does not disappear, will have to be treated at some point and can add significantly to the costs of each District Council in an inequitable way.

8.21 It is also worth noting that in the case of every option shown above the whole of the Authority's General Fund, as well as other funds not yet available, is shown as fully allocated. This is not a financially prudent or practical proposition, the General Fund is required as a form of insurance against unexpected costs, and so a normal balance will need to be identified and maintained.

8.22 The Authority will monitor the financial position very carefully over the next few years to ensure it keeps Levy increases to a minimum. This approach will be predicated upon discussions with District Council Treasurers to ensure that the levy has the least impact possible on the Councils.

9. Capital costs

9.1 The estimated costs of the capital programme are shown at Appendix 3 of the report. The programme largely represents the cost of renewing the Authority's infrastructure to enable it to meet its commitment to Districts to manage the disposal of waste. For 2015-16 the proposed programme has reduced from over £1.481M to £1.414M which reflects the additional time and costs for the Old Swan HWRC, offset by savings elsewhere from minor works some of which have been re-allocated for the Old Swan HWRC.

9.2 The future programme in 2016-17 reflects the diminished financial resources available to the Authority as well as the requirement to complete a strategic review before any further expenditure is approved. The programme includes only basic maintenance and .does not allow for any new developments as none are planned at this stage. Should the strategic review identify any further developments that may be required Members' views and Authority to proceed will be sought at that stage.

10. Budget 2016-17

10.1 The Authority is asked to set a revenue budget of £75,462,31, which reflects the removal of cushioning of £6.073M provided by the Authority in 2015-16, as well as the additional cost pressure from the new HWRC, the cessation of interim contracts and the introduction of the RRC without any significant cost mitigation from potential income sources.

11. Levy 2016-17

11.1 The Levy for 2016-17 proposals is as follows:

- a 1% increase – setting the Levy at £66,247,010

11.2 Once again for 2016-17 the Levy is supported by a significant 'cushioning' contribution from General Fund balances: (£9.215M).

11.3 Members are recommended to accept the 1% increase option at this stage, along with a commitment to a strategic review of waste system costs and a wider agreement that, regardless of the outcome of any strategic review and savings proposals, the overall Levy, expenditure, and reserves will need to be equalised properly in future years.

REVENUE BUDGET 2016-17

1. Introduction

1.1 The Authority is required by statute to set its Levy for 2016-17 by 15th February 2016. In so doing, it needs to consider the financial effects of all factors which impact on the Authority, its Budget, the Levy and the consequential effects on the District Councils on Merseyside. These factors are summarised in the Executive Summary to this report.

1.2 The Authority's Levy calculation is based on its budget estimates and the Local Government Act 2003 which imposes a requirement (under section 25) that:

- 'The Chief Finance officer of the Authority must report to the Authority on the following matters:

  a) the robustness of the estimates made for the purposes of the calculation; and

  b) the adequacy of the proposed financial reserves.'

1.3 The adequacy of the Authority's reserves are considered in paragraphs 3.1 to 3.6 of this part of the report.

1.4 For a number of years the General Fund Reserve was held at a 'higher than normal' level to reflect the potential for significant unforeseen costs arising from the RRC procurement. The procurement concluded two years ago and the Authority's cost pressures were those arising within the existing and prospective contract. As a consequence the General Fund is available to support the Authority's budget over the medium term. The Authority must maintain a reserve to provide security against unforeseen events. Under the budget proposal for 2016-17 the level of General Fund will be maintained at a level that enables the Authority to take account of unplanned events. Over the following two years 2017-18 and 2018-19 the Authority will have to consider the level of General Fund it is able to maintain in the face of significant pressure on the Levy, savings and the possibility of transferring funds remaining in the Capital Fund (an earmarked reserve) to supplement the General Fund will be a decision that Members will need to consider over the next two years.

1.5 The budget proposals reflect cushioning by the Authority of the impact of the budget on the Levy, and therefore on District Councils. This cushioning may still be possible in the medium term through the use of the General Fund over the next three years, including use of anticipated income as surplus funds are released from the Authority's wholly owned company Mersey Waste Holdings Ltd. The risk of this approach is that after the three years in the medium term plan there remains a large gap between the Authority's budget and the Levy.

1.6 Members are being asked to consider this issue in this budget round. The Authority must be prepared to continue to work hard to strip costs out of the budgets where possible; recognising that as most of the Authority's costs are tonnage related a large part of this cost reduction can only be achieved if District Councils reduce the tonnages they provide for the Authority to dispose of. The Authority is also likely to have to consider whether levy rises in this budget round and in the future will enable the Levy income to catch up with the Authority's budgeted costs. Without taking steps to equalise the Levy and expenditure in this budget and forward in the medium term there is a very real prospect, regardless of savings, of a cliff edge Levy increase within the next two years.

1.7 The capital reserve was created to contribute towards the costs of capital schemes offsetting the costs of borrowing. It will support the Capital programme for 2016-17 and for the next two financial years. At this stage the proposed capital programme does not include significant developments as the outcome of the strategic review in not known and may not require further infrastructure development. If the fund is unutilised over time then it may, by a decision of the Authority, revert to supplementing the General Fund, as its source was revenue earmarked for capital purposes, rather than stemming from the sale of capital assets.

1.8 The robustness of the Authority's budget for 2016-17 is considered against a table of components with the Authority's position identified against them.

COMPONENT	COMMENTS
Availability of reliable information	The budget is based on realistic assumptions of pay, price and contract increases and tonnage throughputs to recycling or landfill. This is coupled with an assessment of the major financial risks and how they are to be managed.
Guidance and strategy	The Authority's Financial Procedural Rules cover the management of its budget. The Budget timetable is well communicated and the Strategy is clearly outlined
Corporate approach and integration	Section managers identify budget pressures and risks at an early stage in the process, particularly the financial effects of landfill taxation, changes to waste management contracts and processes as well as litigation risks.
Flexibility	Flexibility in budget management is built into the Authority's Constitution.
Monitoring	The Authority operates a quarterly published monitoring regime, whilst monthly monitoring is undertaken by Section Managers and the Business Support Manager.

1.9 Based on the above arrangements, it is reasonable to consider that the Authority has a robust budget process.

2. Revised Budget 2015-16

2.1 Budget managers work with the Business Support Manager to review and monitor their budgets on a monthly basis identifying trends and any areas of potential under or overspending so that remedial action can be taken where that is necessary. The Authority formally monitors its overall revenue and capital budgets on a quarterly basis through the quarterly performance report and uses this to monitor the position at the end of the third quarter of the year to predict the outturn for the year in a Revised Budget which Members are asked to approve.

2.2 The Revised Revenue Budget for 2015-16 is shown at Appendix 1, in column 2 of the respective pages and details a total cost of £66,145,469 which is a decrease of £1,823k from the Original Revenue Budget for 2015-16 (Column 1 of the respective pages of Appendix 1) which totalled £65,591,099. This decrease has allowed the Treasurer to propose making the following additional adjustments to balances and reserves.

	£000
General Fund – additional contribution from revenue to the Fund	1,823

2.3 The final balance on the General Fund is forecast to be at £16.298M at 31 March 2016.

2.4 The Capital fund will be set aside for funding the Authority's capital programme in the short to medium term, rather than taking out additional borrowings.

2.5 The main areas for saving (-) or increased cost (+) in the Revised Revenue Budget for 2015-16 are as follows:

	£000
Establishment – reduction of £190k in employee costs accompanied by small savings across the budgets; offset by transfer in of the Education budget (£38k) and a reduction in income from Capital fees (£125k) and income from Halton (£17k). A 'support' budget was transferred to closed landfill.	-68
Contracts – savings arising from the increased use of interim contracts (£7.3M) which reduced the costs of disposal contracts (£2.1M) and landfill tax (£6.7M). The income from trade waste was reduced (£226k), the performance improvement	-1,394

budget will be underspent (£105k)	
Closed landfill – minor savings from managing trade effluent and site costs effectively	-5
Rents, rates, depreciation – reductions arising from lower than anticipated impairment costs	-177
Recycling credit payments – lower than expected for all District Councils (Liverpool -£173k, Wirral -£40k, Sefton -£236k, Knowsley -£158k, St Helens -£317k)	-924
Strategy & resources – increase in the expected cost of the waste strategy programme to fund the composition analysis, funded by transfers from other programmes (+91k) offset by reductions in the programmes for Re-use (-£10k) and Waste prevention (-£30k)	+51
Interest – increase in net cost of interest	+209
Capital Adjustment account – technical accounting adjustment to reflect change in depreciation above	-10
Contribution from GF – to support waste strategy review	-5
TOTAL NET DECREASE	-2,323

3. Proposed Budget 2016-17

3.1 The proposed budget for 2015-16 is shown at Appendix 1, in Column 3 of the respective pages, and details a total cost of service of £75,462,311 which is a significant increase on previous years, as a result of changes to contracts and no planned contributions from balances, until the Levy is considered.

3.2 The main reasons for changes to the budget are as follows:

	£000
Establishment – employee costs savings from Redundancy and Retirement with posts taken off the establishment, offset by pay award costs and increases in NICs and pension costs (total reduction £132k), together with by savings from, transport, agency and support costs, offset by an increase in the charge for premises (£80k) and a reduction in capital fee income (£160k) as the capital programme slows down	+52
Contracts – this year is where the transition from landfill and interim contacts is planned to be completed with a move to commissioning and then full operation of the RRC. Contract savings (£9.1M) plus landfill tax savings (£23.8M) offset by the cost of the new contract (£37.3M). Elsewhere performance improvement savings (£79k) are offset by loss on income on Trade Waste (£226k)	+4,589
Closed landfill sites – minor operational savings	-14
Rents, rates & depreciation – small changes in rent and rates accompanied by by an increase in the depreciation charge (£100k) and reduction in the impairment charge (£100k)	-9
Recycling credits – a decrease in demand for recycling credits from all District Councils (Liverpool £193k, Wirral £36k, Sefton £183k, Knowsley £146k, St	-803

Helens £285k)	
Strategy and resources – reductions in the following programmes: Apprentices (£60k no budget remains), Re-use programme ((£20k), Waste Prevention programme (£20k)	-100
Contract review – additional expenditure to support the strategic review – funded from GF contribution	+100 -100
Interest – reduction in interest receivable (£104k) as a result of falling levels of reserves and balances; added to an increase in interest costs (£60k)	+164
Capital adjustment account – technical accounting adjustment	-51
Dividend – Removal of one off income from MWHL as surplus funds are dispersed to the shareholder	+4,000
Contribution from General Fund – removal of the 2015-16 planned contribution from the General Fund (Levy funding to be considered elsewhere)	+2,073
Total	+9,901

3.3 The proposed Revenue Budget for 2016-17 has been prepared on the basis of the following assumptions:

- No inflation unless contractually unavoidable
- 1% pay inflation increase – as agreed through national pay bargaining
- Capital financing costs based on the Capital programme investment as identified at Appendix 3
- That contingency sums are minimal

In addition each of the budgets has been reviewed in detail by budget managers and savings have been identified which have contributed to ensuring the budget is kept to a minimum.

3.4 The Authority's Balances are shown on the second page of Appendix 1 with the various amounts anticipated to be held at 31 March 2017 as follows:

	£M
General reserve	16.198
Capital reserve	2.321

3.5 The General Fund reserve has been applied for the following purposes in 2015-16:

- Support for review of circular economy proposals £5k

3.6 The level of General Reserve has been reviewed as part of the medium term financial strategy. Taking into account the current headline levels of contribution towards either allowing for a modest levy increase or a neutral Levy for 2016-17, and looking ahead into the following two years it is expected that the General Fund will be diminished to a level will be regarded as inadequate unless a combination of savings and modest levy increases continues to take place.

3.7 While the planned balances for 2016-17 remain at reasonable levels in the scenarios considered earlier in this report, the balances for 2017-18 and 2018-19 are less clear and the Authority's financial position on those years is likely to become much more precarious.

3.8 The level of General Fund will be reviewed as part of the strategic review of waste services including the level of savings, expenditure and the Levy strategy over the next year. Only by applying relatively modest Levy increases can the prospect of a cliff edge rise in the levy in 2018-19 be avoided, unless there are very significant cost savings (i.e. the levels of waste delivered to the Authority by Districts diminishes significantly). There will need to be increases in the Levy in the medium term to enable the Authority to close the gap between spending and income.

Risks

Risk	Potential impact	Risk category
Contract commissioning fails and the Authority continues to use Landfill	The impact of this would be to make the Authority vulnerable to price escalation in landfill costs as contractors would no longer be obliged to provide landfill on the same terms as existing contracts	Medium (other large waste contacts elsewhere have suffered delays in commissioning)
Facility fully operation - delays	Additional delays, likely to lead to increased landfill and interim contract costs. If this happens the General Fund remaining balances may need to be utilised to subsidise additional costs.	Medium

4. Capital programme

4.1 The Capital programme is set out at Appendix 3 of the report. The programme represents small but a continuing programme of site works at HWRCs and developments at the closed landfill sites managed by the Authority. There is no significant development planned at this stage as the Authority is planning to be part of a strategic review of waste across Merseyside, following which the need for any further infrastructure developments will be clearer.

4.2 The funding for the capital programme will be through a contribution from the capital reserve before considering an extension of the Authority's Prudential Borrowing, which may be necessary to complete the programme in 2017/18.The impact of the existing prudential borrowing is set out in an annex to the Treasury Management Strategy Statement 2016/2017 elsewhere on this agenda.

5. The Levy

5.1 The Authority is required under section 74 of the Local Government Finance Act 1988, as amended, to issue its Levy demands upon the District Councils of Merseyside before 15 February each year.

5.2 The Levy is made by the issue of demands stating the dates on which instalment payments are to be made and the amount of each instalment. For the purpose of standardisation it is recommended that the Levy be paid by way of ten equal instalments on the following dates, in line with the Levying Bodies (General) Regulations 1992 payment schedules:

14 April 2016	20 October 2016
26 May 2016	24 November 2016
7 July 2016	5 January 2017
11 August 2016	9 February 2017
15 September 2016	16 March 2017

5.3 The Levy proposals are shown in the tables below. For each of the constituent Districts there are changes in the levy demand, as calculated through the levy apportionment methodology.

5.4 Members will recall that the levy apportionment methodology is based in the ‘polluter pays’ principle which means that tonnage based costs are based on the last full financial year’s tonnages (subsequently adjusted to actual in the year), and the balance of costs is apportioned on estimated population.

5.5 The proposed levy for 2016-17 for each District is shown below, with comparisons to 2015-16. Further Levy options are shown in Appendix 2, but the recommended Levy increase of 1% in 2016-17 is the only option shown in the body of the report. The methodology used to establish the District Levy is attached at Appendix 4.

1% Levy increase

District	Levy 2015-16 £	Proposed Levy 2016-17 £	Change £	Change %
Knowsley	7,075,562	7,284,091	208,529	2.9
Liverpool	22,383,549	23,007,146	622,597	2.8
St Helens	8,139,758	7,442,787	-696,971	-8.6
Sefton	12,461,387	12,960,833	499,446	4.0
Wirral	15,530,841	15,533,157	22,314	0.1
	65,591,098	**66,247,014**	**655,915**	**1.0**

5.6 The Recommended Levy is an overall 1% increase. Further increases above this Levy will be needed in future years, regardless of savings and efficiencies, to ensure the Authority's financial position is secure.

6. Risk Implications

6.1 The Authority's budgeted costs continue to increase as the vast majority are waste tonnage related, and there is no reduction in the tonnes the Authority is required to process. At a time when the financial pressure on constituent District Councils is severe, it is incumbent upon the Authority to mitigate the impact of the Levy as much as possible. For 2016-17 and beyond it is possible to utilise the Authority's reserves and additional income to mitigate the impact of the Levy and to keep Levy increases to modest levels. However, in the longer term there will remain a budget gap that requires closing, probably through a combination of cost reduction where possible, prudent use of reserves and in all likelihood modest increases in the Levy going forward. If the option to reduce the Levy is taken then this risk is increased significantly and the need for a very drastic Levy increase in the next two years will become a reality.

6.2 In planning for savings the Authority will also take a risk, particularly where savings proposals involve reducing or removing services, and especially if those are services based in HWRCs that the full impact of savings may not be achieved in the year. This could be a particular risk where service reductions require consultation to take place and will depend to some extent upon the outcome of that consultation.

7. HR Implications

7.1 There are no HR implications in this report

8. Environmental Implications

8.1 There are no new environmental implications arising from this report, although it does cover the period when the Authority makes the transition from Landfill to the new Resource Recovery Contract.

9. Financial Implications

9.1 The financial implications run throughout this report.

10. Legal Implications

10.1 The Authority is setting a budget for 2016-17 which ensures there is sufficient income and resource to cover budgeted expenditure. Looking into the future decisions about how that will continue to be achieved will need to be made.

11. Conclusion

11.1 The Authority is required to establish and approve a budget for 2016-17 ad to set a Levy for the same period that it applies to the constituent District Councils. The report and its appendices and recommendations enable Members to consider and approve the proposed budget and Levy.

11.2 Members are also asked to consider and approve the proposed capital programme.

The contact officer for this report is: Peter Williams
7th Floor, Number 1 Mann Island, Liverpool, L3 1BP

Email: peter.williams@merseysidewda.gov.uk
Tel: 0151 255 2542
Fax: 0151 227 1848

The background documents to this report are open to inspection in accordance with Section 100D of The Local Government Act 1972 - Nil.