



St. Helens Council

# Internal Audit Report 2017/18

## Merseyside Recycling and Waste Authority Resource Recovery Contract

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## St. Helens Council

### **Merseyside Recycling and Waste Authority Resource Recovery Contract**

#### **1.1 Introduction**

An audit review of the management arrangements in place for the Resource Recovery Contract (RRC) was undertaken as part of the 2017/18 Internal Audit Plan. The purpose of the Audit was to provide an assessment of the adequacy of the control environment established, to ensure that objectives are achieved and risks are adequately managed.

#### **1.2 Scope**

The review considered the arrangements in place to ensure that payments made are in accordance with the contract and that performance monitoring and reporting mechanisms are robust.

#### **1.3 Background**

##### **Context**

MRWA have a contract with Merseyside Energy Recovery Ltd (MERL) for the operation of the Resource Recovery Contract which is sub-contracted to Suez.

The approved budget for the RRC contract is just in excess of £40m per annum.

The operation of the contract consists of municipal residual waste being delivered to the Rail Transfer Loading Station (RTLS) at Kirkby for transfer to the Energy from Waste (EfW) plant at Wilton on Teeside; with the exception of occasional contingency disposal arrangements coming into force for planned or emergency shutdown of the EfW plant.

The RTLS and the EfW plant at Wilton became fully operational with effect from 1<sup>st</sup> September 2017.

## 1.4 Audit Opinion

Internal Audit contribute to the overall governance of the Authority by providing an opinion on how effectively risks are being managed and the adequacy and effectiveness of internal control in relation to the areas under review.

Our opinion is based on the work performed as described in the above scope, which was agreed with management prior to the commencement of the review.

Our overall opinion, following this review is as follows:

### **Substantial Assurance**

The majority of expected controls are in place but there is some inconsistency in their application. Whilst there is basically a sound system of controls, there may be weaknesses in the design and/or operation of these and recommendations have been made to enhance the control environment further.

A number of recommendations were made verbally during the course of the audit and prompt action was taken by management to address the related issues. Consequently, there is no requirement to include them in an Action Plan. Whilst evidence of action taken was provided to us, continued compliance will be subject to assessment during the next audit review of the RRC.

## 1.5 Key Issues

There are no key issues arising from this review.

## 1.6 Agreed Action

No recommendations have been made following this review.

## Control Objectives 2

### **Merseyside Recycling and Waste Authority**

#### **Resource Recovery Contract**

**To gain assurance that the following control objectives are being achieved within an appropriate framework of control:**

1. To confirm that contract payments are in accordance with the Payment Mechanism and are accurate, legitimate and accounted for appropriately
2. To ensure that appropriate and effective contract monitoring arrangements have been established and enforced.
3. To ensure that appropriate and effective budget and performance monitoring arrangements are in place.

## Findings & Conclusions 3

### Findings

**3.1 Control Objective: To confirm that contract payments are in accordance with the Payment Mechanism and are accurate, legitimate and accounted for appropriately.**

We established that nine out of ten expected controls under review were in place and working effectively.

However, weakness in the design or operation of one control was identified. This related to the underlying calculation of the Fuel Indexation Rate that forms part of the Payment Mechanism. The error in the calculation had also been identified by the contractor, Suez. We were informed that MRWA and Suez are in consultation over the matter and resolution is currently being sought. On this basis, no recommendation is necessary. It is planned for the outcome of this matter to be reviewed during the next audit of the RRC.

Payments are made monthly under the terms of the Contract. Whilst the monthly payments are largely based on annual tonnage forecasts, there is provision for quarterly and annual adjustments to take into account variances against actual throughput. We examined a sample of three months payments since the contract became fully operational. This included a review of a quarterly adjustment.

We confirmed that there are processes in place to verify the supporting data and challenge any discrepancies with the Contractor. We established that other than for the implication of the Fuel Indexation Rate referred to above, the payments were accurate, fully supported by base data and in accordance with the Payment Mechanism Schedule of the Contract. We verified that the payments had been appropriately certified and that a clear segregation of duties had been applied.

No recommendations have been made.

**3.2 Control Objective: To ensure that appropriate and effective contract monitoring arrangements have been established and enforced.**

We established that five out of seven expected controls under review were in place and working effectively.

However, weaknesses in the design or operation of two controls were identified.

The Contract is essentially a self-monitoring contract. In accordance with Schedule 17: Performance Mechanism, the Contractor is required to report any failures in respect of a prescribed range of Key Performance Indicators (KPI's). In addition to this, there are quality assurance checks performed by MRWA on the data submitted by the Contractor in order to establish if there are any failures that have not been notified by the Contractor. Any KPI failures, including failures to report, are subject to performance deductions. We confirmed that the KPI's have been appropriately monitored and performance deductions generally applied when applicable. There are instances, however, of KPI's being in dispute with regards to interpretation of how they are to be applied. As these are currently under consideration by MRWA management, with a view to resolution being imminent, there is no recommendation necessary to address the matter. The outcome will be examined in the next Audit Review.

Site visits to the Wilton plant were undertaken on a regular basis during the commissioning phase. It was envisaged that once the RRC became fully operational a consultant would be

appointed to undertake inspections of the Wilton plant to ensure that facilities are managed, operated and maintained in full accordance with technical specifications and contractual obligations to ensure performance at an optimum level. However, due to the cost of an external consultant being prohibitive, a decision was taken to undertake this role in-house, as much as is practicably possible. A contract monitoring framework should be in place to define roles and responsibilities, monitoring criteria and frequency of inspection. Consequently, during the course of the audit, contract monitoring procedures were drafted for the Wilton Plant and also the RTLS. Compliance with these contract monitoring procedures will be assessed during the next Audit Review.

Regular, monthly contract meetings are held with the contractor which provide the facility for issues raised from contract monitoring visits to be raised and appropriately addressed.

No recommendations have been made.

### **3.3 Control Objective: To ensure that appropriate and effective budget and performance monitoring arrangements are in place.**

We established that all expected controls under review were in place and working effectively.

It was confirmed that the Quarterly Performance Monitoring Reporting mechanism provides updates on the RRC contract to the Executive Management Team. These reports provide for key issues and the budget position to be reported. As a consequence of the interim landfill arrangements that were necessary due to the delays associated with the contract becoming fully operational, there was a projected overspend for 2017/18 on the transport element of the Waste Management & Recycling Contract (WMRC) budget, estimated to be approximately £400k (at the time of writing). We are informed that this overspend was managed within the budgetary constraints of the overall waste management contracts budget.

We confirmed that there were regular update reports provided to the Authority during the period of delay leading up to the contract being fully operational from 1st September 2017. It is intended that an Annual Report on the RRC will be provided to the Authority for the lifetime of the contract, in addition to reports being provided as and when specific issues arise.

No recommendations have been made.

## Conclusions

Internal Audit contribute to the overall governance of the Authority by providing an opinion on how effectively risks are being managed and the adequacy and effectiveness of internal control in relations to the areas under review. Our opinion is based on the findings of the work performed as described above.

Our overall opinion, following this review is as follows:

### High Assurance

All expected controls are in place and being applied consistently and effectively and there is a sound system of control designed to ensure the achievement of the service or system's business objectives.

### Substantial Assurance



The majority of expected controls are in place but there is some inconsistency in their application. Whilst there is basically a sound system of controls, there may be weaknesses in the design and/or operation of these and recommendations have been made to enhance the control environment further.

### Limited Assurance

A number of expected controls do not exist or are not applied consistently or effectively. There are weaknesses in the design or operation of controls that could impact upon achievement of the service or system's business objectives and these may have resulted in the emergence of key issues.

### Minimal Assurance

A significant number of expected controls are not in place or there are significant weaknesses in the control system that may put the service or system's business objectives at risk. A number of recommendations have been made and / or key issues identified.

