



**London Borough of Hammersmith & Fulham**

**CABINET**

**11 NOVEMBER 2013**

**POTENTIAL EXTENSION OF SERCO WASTE CONTRACT**

**Report of the Deputy Leader and Cabinet Member for Residents Services – Councillor Greg Smith.**

**Open report**

A separate report on the exempt Cabinet agenda provides additional exempt information about the costs and affordability of the contract.

**Classification - For Decision**

**Key Decision: Yes**

**Wards Affected: All**

**Accountable Executive Director:** Lyn Carpenter, Executive Director of Bi-borough Environment, Leisure & Residents Services

**Report Authors:** Sue Harris, Director for Cleaner, Greener & Cultural Services & Kathy May, Bi-borough Head of Waste and Street Enforcement

**Contact Details:**

[sue.harris@lbjf.gov.uk](mailto:sue.harris@lbjf.gov.uk)  
020-8753-4295

[kathy.may@rbkc.gov.uk](mailto:kathy.may@rbkc.gov.uk)  
020-7341-5616

**1. EXECUTIVE SUMMARY**

- 1.1. This report recommends extending the Council's contract with Serco for Waste and Street Cleansing services until 2021. The current contract is due to expire in June 2015, but can be extended if beneficial and agreed by both parties.
- 1.2. The proposed extension will be subject to a revised specification with variations to reflect lessons learnt in the first five years of operating the contract. The extension, as envisaged in the original procurement, will be subject to the Council varying the extant contract with Serco for optimising the services. The implications of, and rationale for, extending the contract are set out in this report, with a summary of the key changes, their implementation, timeframes and implications provided below, in table format, in paragraph 5.1 of this report. Further details of the revised arrangements, their annual costs, potential risks and mitigating actions are reported

on the exempt part of the agenda due to their commercially sensitive and confidential nature.

- 1.3 In order to strike a balance between high quality standards of service and value for money, a number of variations to the existing specification are proposed. It is anticipated that the changes will ensure a minimum impact on the high standards of street cleanliness in the borough but by altering the specification to be more output driven, this will enable Serco to be flexible with resources to maximise value for money. Suggested revisions include changes to specification that will give Serco the flexibility to achieve these objectives. These will include:

- cleansing frequency and standards
- waste collection route changes (which would mean collection day changes for some residents),
- changes to working hours,
- reduction in vehicles and crew numbers, and
- sickness reduction.

The aim is still to strive for high standards, but there are risks which are explained in this report.

- 1.4 Research has been undertaken to establish some other authorities' findings when they have gone out to retender a waste and street cleansing contract in order to assist the Council's assessment of benefits and disadvantages of re-procuring a new contract versus agreeing to an extension. A comparison of unit costs has also been possible on a Bi Borough basis. On balance, it is believed that an extension to the existing contract offers a balance between best value for money and on-going quality of service, for the reasons set out in section 6 of this report.
- 1.5 Heads of Terms are being completed to reflect the proposed new revised arrangements with Serco.

## **2. RECOMMENDATIONS**

- 2.1 That officers be instructed to negotiate terms of a possible contract extension, including variations, with Serco as in the report on the exempt part of this agenda.
- 2.2 That the extension end date be 2021, which would then be co-terminous with the Royal Borough of Kensington and Chelsea contract end date
- 2.3 That the Leader and the Cabinet Member for Resident Services, in consultation with the Executive Director for Environment, Leisure and Resident Services, approve any revised contractual terms.
- 2.4 That a further report to be submitted for approval if required.

## **3. REASONS FOR DECISION**

- 3.1 The options regarding extending the contract versus going out to tender have been carefully considered. This has been done with the support of London Waste and

Recycling Board's efficiency programme utilising the expertise of Eunomia Research & Consulting Ltd, who are technical experts in this field.

#### **4. INTRODUCTION AND BACKGROUND**

- 4.1 The Council and Serco have been in the process of renegotiating the terms for a potential contract extension of the waste collection and street cleansing contract beyond the break clause date of June 2015, as is permitted within the existing contract arrangements. H&F has been assisted in both the financial and technical analysis of a contract extension by Eunomia Research & Consulting Ltd, appointed by The London Waste and Recycling Board (LWARB). A decision on whether or not to utilise the extension option within the existing contract must be taken in this calendar year to ensure that if the retender option is to be followed, there is enough time for a full procurement exercise to be both completed and a new contract fully mobilised before the 2015 deadline.
- 4.2 The proposal to extend the Serco contract is for a period of 6 years and not the 7 years permitted in the current arrangements as this would ensure the end date of 2021 was co-terminous with that of the Royal Borough of Kensington and Chelsea's waste and street cleaning contract with Sita. The opportunity for one contract across the Bi-borough area could potentially result in greater future efficiencies.
- 4.3 A series of efficiencies have been agreed that require only a limited number of specification changes, and changes in working practice within the current terms of the contract. These are summarised below. The achievement of these savings would be entirely at Serco's financial risk. In implementing the above, Serco have committed to efficiency savings which will allow them to deliver a high quality service that is economically sustainable for both parties. There are also opportunities to bring forward some elements of the revisions to allow for savings to commence earlier than June 2015, as outlined below in paragraph 5.1.
- 4.4 Recognising that Members require assurance that the Council would receive value for money from the proposed extension, Members should note that there are also areas of service enhancements that would be delivered through the extension. The enhancements extend the scope of cleansing in areas that would previously not have received additional cleansing or were not formally recognised within the contract. For example, the tops of side roads at junctions with high visibility roads would receive a daily cleanse for up to 25 metres which was never included in the original contract. Also, to reflect the changing demographics of the borough, cleansing schedules will be increased to twice-weekly on some residential, high footfall roads.

#### **5. PROPOSALS AND ISSUES**

- 5.1. The proposed features, associated issues and risks are described in the table below, and explored more fully in Appendix 2 of the report on the exempt part of the Cabinet agenda:

	Item	Implementation plan	Potential Timeframe	Implications
	<b>Collections</b>			
1.	Refuse & recycling productivity	Re allocate work onto 11 rounds, minor day changes Mon/Tues	Pre Dec 13	May impact on industrial relations, loss of good will etc.
2.	<b>General</b>			
3.	Supervisor reduction	Rationalise role of Supervisor	Mar/Apr/2014	Cleansing standards/ redundancy cost
4.	<b>Streets</b>			
5.	Spec - restore to grade	Discuss and agree reduced response times to restore cleaning grade. Savings may be greater or less depending upon H&F requirements	As soon as agreed	
6.	Spec - cleansing frequencies	Discuss and agree white roads cleansing that may hold up to once a week/ red roads review Savings may be greater or less depending upon H&F requirements	Summer 2014	Will also take account of requirement for increased cleansing in some areas
7.	Clean season	Following changes 5 & 6 above to evaluate further reduction in resources during the winter period	tbc	Will need to review following items 5&6
8.	<b>Collections</b>			
9.	Bulk productivity bins	Need external consultants to optimise routes (cost taken account of) Additional drivers' hours/relaxation of operating hours to allow double shifting (estates) Serco to manage beat sheets	Autumn 2014	Short term increase in complaints
10.	<b>Labour Cost</b>			
11.	Sickness management	More robust implementation of procedure and less risk averse	To commence ASAP	New starters do not get paid for first 3 days of any period of sickness so cost benefit reduced

## 6. OPTIONS AND ANALYSIS OF OPTIONS

### Advantages and disadvantages of extending versus re-procurement

- 6.1 As previously reported to Members in July 2013, the key option is whether to extend the Serco contract beyond 2015, or to re-procure the services.

- 6.2 A summary of the proposals from Serco, which officers have been discussing with Eunomia Research & Consulting - experts in waste and recycling and street cleansing contract procurement - along with advice received from Eunomia on the option of re-procuring, is presented below:
- i. The municipal environmental services market is highly competitive at the current time. Recent experience suggests that it is very difficult to win a typical municipal collection contract without under-resourcing the bid in order to reduce price. This risk can be mitigated but not eliminated by carefully designing the procurement process to avoid this outcome.
  - ii. Given the apparently loss making nature of the current contract for Serco, it is arguable that the key risk for H&F is less the lack of opportunity to make savings than the risk of a significantly under-resourced bid from a contractor who does not have an in-depth understanding of the local operational issues.
  - iii. Any procurement would need to be well-planned and executed to maximise the level of competition and potential for price constraint yet avoid jeopardising service quality.
  - iv. One issue for the Council in seeking to ensure a good price is the issue of contract term; procuring a new contract that would expire at the same time as the existing RBKC contract would necessitate a six year contract. (It would also mean commencing a regulated competition for a 2021 Bi-borough arrangement four-and-half years in to a new H&F contract.) Environmental services contracts are typically seven to eight years as a minimum to allow for reasonable depreciation of collection assets (mainly vehicles). A shorter contract risks contractors incurring additional costs which would be likely to be passed on in the tendered price.
  - v. The costs to the Authority of a re-procurement exercise would not be insubstantial; H&F could consider the use of the IESE Waste Management Services Framework to reduce procurement costs, however it is important to note that whilst the framework has been open for over a year, to date there have been no major waste and recycling contracts procured using it. To this extent the potential savings of going down this route are as yet untested.
  - vi. A reasonably conservative estimate of the likely costs that H&F could expect to incur for a non-framework procurement exercise is £200k-£300k (including external technical and legal advice and officer time).
  - vii. H&F is currently benefiting from a relatively well-performing service with good levels of customer and Member satisfaction. Any transition from old to new contractor, however well managed, is likely to lead to some (hopefully short-lived) disruption to service, not least since cost savings are likely to be delivered through rationalisation of resources.
  - viii. The potential for a degree of (albeit short-term) disruption to service performance is, therefore, another consideration when weighing up the potential benefits of achieving significant cost savings through retendering. There is also the consideration that re-tendering is likely to lead to a need to repeat, to some extent at least, the hard work already invested in developing the current contract management relationship with Serco.

- 6.3 Officer contact with other London authorities has confirmed that the current market is very competitive, with the difference between the highest and lowest being very close in percentage terms, particularly where a very comprehensive and detailed specification is provided. Although, many companies are expressing an initial interest and submitting PQQ's, few are submitting final bids, which indicates a wariness to enter into a contract where risk could be high.
- 6.4 Some Bi-Borough cost benchmarking has been possible and is reported on the exempt part of this agenda.

## **7. PROPOSED TERMS**

### **Contract expiry**

- 7.1 The expiry of the extension would be co-terminous with the expiry of the RBKC SITA contract in 2021, allowing for a joint procurement of services by the two boroughs at that time. This means that the extended Serco contract term is reduced from 7 to 6 years.

### **Specification changes**

- 7.2 The efficiency-led specification changes and risks are outlined in Appendix 2 of the report on the exempt part of this agenda.

### **Deed of Variation**

- 7.3 Both the Council and Serco have agreed to incorporate the content of the deed of variation proposed by the Council in 2012 within the new extension variation. This variation made some specification changes relating to collections from, for example, mansion blocks, and bulky waste, WEEE and special collection services. The majority of the specification changes within this deed of variation have already been enacted by Serco.

### **Future savings share**

- 7.4 In addition to the efficiency savings already identified by Serco, the terms of the extension will require the Contractor to seek to identify further savings on an annual basis. Where such further savings are made then these will be shared on a 70/30 basis in favour of the Council. Such savings will be discussed, planned and agreed via the proposed Improvement and Efficiency Board, and will be factored in to future year savings proposals.

### **Cost monitoring**

- 7.5 Currently, service costs are monitored using a Bill of Quantities approach. This approach does not provide for the level of scrutiny of actual costs incurred by the Contractor and, in addition, does not allow the desired flexibility to be able to accurately identify the impacts on real costs of future service changes (including those that may be required due to future budgetary pressures). For this reason, the extension will also allow for the Council and Serco to adopt a new form of contract cost monitoring based on a detailed contract cost reporting process. Transparent contract cost reports will be provided by Serco that better reflect the true apportionment of costs between services. In reality many resources are shared across a number of services and the contract cost report will provide a detailed

schedule of actual costs for the resources deployed, alongside details of the services undertaken by each resource.

### **Street Cleansing Performance Incentive Mechanism**

- 7.6 A new incentive mechanism will be agreed to incentivise the Contractor to meet or exceed the required street cleansing standards. This will involve a financial reward per year paid to the Contractor in the event that it exceeds a benchmark performance standard. Where the independent survey confirms that cleansing standards have not been met, the Council will have the right to deduct up to the reward amount from payments to the Contractor per year. The measurement of performance shall be via the independent street cleansing survey which is carried out three times per year; therefore the reward or deduction will be paid on the basis of one third for each survey. The details of the benchmark against which Serco's performance is to be measured is yet to be agreed but it will relate to an average performance standard achieved by Serco over a number of previous years, yet to be agreed (financial figures are in the exempt report). This is a new feature of the contract and therefore a budget would need to be set aside within the overall contract budget in order to accommodate this should Serco meet or exceed the standards.

### **Additional services**

- 7.7 In addition to the existing core services delivered by Serco, officers are exploring the possibility of including a small number of related services that are currently delivered in-house within the extension. These are:
- Graffiti removal
  - Clinical
  - Litter bin installation.

Should the price offered by Serco for any of these services represent a saving for the Council, when compared with current service costs or alternative service provision business cases already prepared, then the service will be included within the scope of the extension, subject to legal advice at the time.

### **Other considerations**

- 7.8 It is anticipated that, over the next 12 months, H&F will decide on the future potential use of Bagley's Lane depot; this could involve relocating temporarily or permanently, and securing the site's redevelopment either with a replacement depot in situ or by securing a replacement depot elsewhere. Such moves could start within that time frame if a decision is taken to move early. Serco are aware of these potential plans and could be considered well placed to respond to any requirement for flexibility. Any additional costs associated with a move from their current operational base are not factored in to this report.

### **Recycling - 'TEEP'**

- 7.9 From 1 January 2015, waste collection authorities will be required to collect paper, metal, glass and plastics separately from source rather than in a co-mingled collection, as is the case at present. Co-mingled collection will only be an option if it is not 'Technically, Environmentally and Economically Practicable' (TEEP) to switch to separate collection. This arises from the Waste (England and Wales) (Amendment) Regulations 2012 which were introduced to comply with the 2010 revision to the Waste Framework Directive. Local Authorities are awaiting formal

advice from Defra which is expected around November this year. Officers will feed back to the Cabinet Member for Residents Services shortly on any implications, discuss such implications with Serco, and report back to Cabinet if necessary,

## **8. CONSULTATION**

- 8.1 The usual internal consultations will have taken place including consideration at the Bi Borough Procurement Board. External consultation is not deemed practical or necessary for such a contract review. However, as part of the waste and street scene enforcement review, the views of customers are being gathered and will inform this process. External challenge has been provided via Eunomia's review, the cost of which is to be paid once the savings are delivered. This is expected to be funded from an invest-to-save bid, which will be repaid in year one of the extended contract.

## **9. EQUALITY IMPLICATIONS**

- 9.1 The recommendations in this report have no impact on the public sector equality duty. Should potential issues arise from service changes (for example, any changes to days of collection or cleansing close to places of worship, or potential impacts of changes to frequency of collections for or near to residential care homes), these can be dealt with at the time, as would normally be the case for such changes. Such potential issues will be raised as part of the further negotiations with SERCO.

Comments verified by Carly Fry, H&F Opportunities Manager. Tel 020-8753-3430.

## **10. LEGAL IMPLICATIONS**

- 10.1 The present contract extension proposal is subject to compliance with Public Contracts Regulations. In principle, if the variations being proposed in the service specification were envisaged as part of the original procurement and do not materially alter the nature of the contract so as to form the subject matter of a new contract and procurement, then these would be permissible. These variations are still being negotiated and so a definitive view cannot be made but going by the proposed changes mentioned in the appendix 2 to the Exempt version of this report, it would appear that these proposed changes may not be seen as material amendments to the contract and the risk of successful challenges may be remote.

Implications verified/completed by: Babul Mukherjee, Solicitor (Contracts) Bi-Borough Legal Services Team, RBKC, 020736

## **11. FINANCIAL AND RESOURCES IMPLICATIONS**

- 11.1 In addition to the current fixed annual cost of the waste and street cleansing contract, the Council incurs variable charges, including an amount for services relating to commercial waste which is passed on to customers through fees and charges (details in the exempt report). Equivalent amounts are included in the existing departmental revenue budget for the waste and street cleansing service. An increase in the fixed contract sum that would increase the fixed contract cost per annum is not currently included in the departmental revenue budget and will be requested as budget growth as part of the 2015/16 Medium Term Financial Strategy (MTFS). This



growth requirement has also been included as a pipeline growth bid for 2015/16 as part of the 2014/15 MTFs process at the original (higher) amount. It is expected that the cost reductions and efficiencies identified by Eunomia and Serco, as set out in this report, will contribute to the ELRS MTFs savings target for 2015/16. Further detail and analysis of the financial implications of the proposed extension and associated changes are reported on the exempt part of this agenda due to their commercial sensitivity.

- 11.2 Implications verified/completed by: Mark Jones, Director for Finance TTS and ELRS, telephone number 020 8753 6700

## **12. RISK MANAGEMENT**

- 12.1 It has been made clear in the report that given the current value of the contract to Serco, they would not continue beyond 2015 under existing terms. This risk, including options to re-tender, have been carefully considered in liaison with Officers and Eunomia. The options presented inevitably come with an element of risk, however the proposals also present new opportunities that include a new incentive payment mechanism for meeting street cleaning standards, options to include existing in-house services in the extension and the future alignment of contracts with the Royal Borough of Kensington and Chelsea. Where service provision changes either in volume or quality on the street there may be some negative risk impact as the public's expectations is against current provision levels and coverage. As the terms of the extension will require the Contractor to seek to identify further savings on an annual basis and, where such further savings are made, then these will be shared on a 70/30 basis in favour of the Council contributing to the management of budget risks.
- 12.2 Whilst the contractor is responsible for risk management on the ground the Environment, Leisure and Resident Services Department is responsible for contract management and procurement risk and they have set out the proposals with risk considered throughout.
- 12.3 Implications completed by: Mike Sloniowski, Bi-Borough Risk Manager, 0208 753 2587

## **13. PROCUREMENT AND IT STRATEGY IMPLICATIONS**

- 13.1 The Director of Procurement and IT Strategy supports the report's recommendations: extending the Council's contract with Serco for refuse collection and street cleansing services so that it aligns with RBK&C's contract, and thereby facilitates a future joint procurement and possible shared service; incentivising the contract; and varying it to improve value for money. These proposals were discussed by the Bi-Borough Procurement Board at its 19<sup>th</sup> September meeting where, after considering a number of implications, they were approved for Member consideration.
- 13.2 A key  
judgement concerns the current state of the market (which at some point the Council will have to re-visit), and whether H&F would get a better deal from others in it than

the one currently being offered by Serco for a 6-year contract extension? The report authors and the external consultant's advise that "the market is highly competitive at the current time". This though needs to be weighed against the risk of such competitiveness resulting in under-resourced bids being returned, with a consequential decline in service quality and resident satisfaction – both of which in H&F are currently high and amongst the best in London. On balance, it is likely that the best possible available outcome – for residents and the Council - will be delivered through a future joint procurement and shared service with RBK&C. In order to achieve this, the Director of Procurement and IT Strategy supports extending the current contract with Serco, subject to the improvements being agreed with Serco and at the cost reported on the exempt part of the agenda.

- 13.3 Implications completed by: John Francis, Principal Consultant, H&F Corporate Procurement 020 8753-2582.

**LOCAL GOVERNMENT ACT 2000**  
**LIST OF BACKGROUND PAPERS USED IN PREPARING THIS REPORT**

<b>No.</b>	<b>Description of Background Papers</b>	<b>Name/Ext of holder of file/copy</b>	<b>Department/ Location</b>
1.	Phase 2 Efficiency Review – Summary of Interim Findings for London Borough of Hammersmith and Fulham	Kathy May	CGCS

**LIST OF APPENDICES:**

- Appendix 1 - Current classification of roads  
Appendix 2 - Proposed street cleansing grade levels, and restoration times