

Report to:	Cabinet	Date of Meeting:	9 January 2020
Subject:	Purchase of Winter Service Facility		
Report of:	Head of Highways & Public Protection	Wards Affected:	(All Wards);
Portfolio:	Cabinet Member - Localities		
Is this a Key Decision:	Yes	Included in Forward Plan:	Yes
Exempt / Confidential Report:	No		

Summary

To seek approval for the Chief Legal and Democratic Officer in conjunction with the Head of Highways and Public Protection to enter into an agreement to purchase the depot currently used to deliver the winter gritting service (winter service facility), located at Heysham Road, Netherton from the existing term maintenance contractor and agree an extension to the existing contract. This facility has replaced the previous council owned facility which was no longer fit for purpose as it did not meet the requirements of the Council's statutory duty and could now be disposed of.

Recommendation(s):

It is recommended that:

- (1) The Chief Legal and Democratic Officer in conjunction with the Head of Highways and Public Protection be authorised to enter into an agreement to purchase the winter service facility located at Heysham Road, Netherton from the existing term maintenance contractor (Graysons H&E Services) as detailed within this report.
- (2) The Chief Legal and Democratic Officer in conjunction with the Head of Highways and Public Protection be authorised to vary the existing contract to include a 20% reduction in tendered rates, as agreed with the existing contractor and extends the existing winter service contract for a period of 4 years. Provision for this extension is included within the existing contract.
- (3) The Head of Corporate Resources in conjunction with the Head of Highways and Public Protection be authorised to dispose of the council owned site of the former winter facility on Damfield Lane, Maghull in accordance with the Council's Asset disposal policy.

Reasons for the Recommendation(s):

The purchase of the facility will save revenue funding over the remaining 9 years of the existing contract and allow the Council to consider alternative methods of procuring or providing the statutory winter service after that point, including bringing the service in-house.

Alternative Options Considered and Rejected: (including any Risk Implications)

The alternative is not to purchase the facility and therefore not take advantage of the revenue rate reductions offered by the contractor. Furthermore, at the completion of the existing contract, the Council will have to re-procure the contract to include the provision of a winter facility, thus potentially paying for the facility twice.

Based on the above and the financial analysis contained within the report, the ‘do nothing’ option would place the Council in an adverse financial position due to the need to contract its own facility and fail to take advantage of the 20% revenue savings.

A further option would be for the Council to build its own facility at the end of the contract which would be excessively expensive in comparison to the proposed recommendation in this report.

What will it cost and how will it be financed?

(A) Revenue Costs

There will be a 20% saving on revenue rates for the remainder of the contract. This is estimated at £191k per annum based historical activity. This level of saving would cover the associated borrowing and increased facility costs of this proposal.

(B) Capital Costs

There will be a capital cost of £2.6m. This will be funded from Public Works Loan Board borrowing. The period of borrowing will be linked to the useful life of the asset, 25 years, and will be met by the annual saving on contract rates and thus will be contained within the services revenue budget.

Implications of the Proposals:

Resource Implications (Financial, IT, Staffing and Assets): All resource implications are detailed in the main body of the report
Legal Implications: See body of report
Equality Implications: There are no equality implications.

Contribution to the Council’s Core Purpose:

Protect the most vulnerable: Not applicable
Facilitate confident and resilient communities: Not applicable
Commission, broker and provide core services: This proposal strengthens the Council’s resilience as, in the event of provider failure, it will own a fit for purpose facility from which an alternative provider could deliver the service from. It will allow the Council to procure the service in future without the cost of provision of a facility or to bring the service in-house.
Place – leadership and influencer: Not applicable

Drivers of change and reform: Not applicable
Facilitate sustainable economic prosperity: The Council will be able to dispose of the previous facility for redevelopment, as it is no longer fit for purpose in accordance with statutory guidance. That land is identified as a housing site within the Local Plan.
Greater income for social investment: The proposal includes a reduction in revenue rates paid to the contractor of 20% which would potentially cover associated borrowing and increased facility costs.
Cleaner Greener Not applicable

What consultations have taken place on the proposals and when?

(A) Internal Consultations

The Head of Corporate Resources (FD5886/19) has been consulted and comments and views have been included within this report.

The Chief Legal and Democratic Officer (LD4070/19) has been consulted and comments and views have been included within this report.

There have also been internal consultations with Executive Directors and property colleagues to ensure the robustness of the proposal.

(B) External Consultations

Discussions have taken place with the service contractor who is supportive of this proposal

Following the expiry of the “call-in” period for the Cabinet Member decision.

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Appendices:

None.

Background Papers:

There are no background papers available for inspection.

1.0 Background

1.1 The Council has historically operated its own winter service facility based at Damfield Lane, Maghull (at the junction with A59 Northway). In 2013, the

Government introduced additional statutory guidance which is extremely complex and includes a revised requirement for the storage of reserve salt stocks to improve the Council's resilience in extreme weather conditions.

- 1.2 The Council's existing facility became unsuitable at this point as it is of insufficient size to accommodate the increased stocks. The service contractor has stored the additional salt at their own premises since that time in order that the Council meets its statutory requirements.
- 1.3 Due to the above, when the Council retendered the winter service contract, it included the provision of a purpose-built facility which would meet the requirements of the statutory guidance and protect the Council from risk.
- 1.4 The contract has been awarded for 6 years with a possible extension of up to 4 years (4 x 1). The new facility is located on Heysham Road Bootle.

2.0 Proposal

- 2.1 It is proposed to purchase the newly built winter service facility from the service contractor. This has been discussed with the contractor who is amiable to sell the facility subject to the Council confirming the full contract extension (4 years) now. As a result, the contract will run for 10 years from the start date in 2018. As part of this proposal the contractor has agreed to reduce his tendered rates by 20%, subject to contractual price fluctuation clauses. Such clauses are common to all Engineering Contracts let by the Council and any fluctuations are traditionally contained within revenue budget allocations.
- 2.2 The incumbent contractor has delivered this service to the Council constantly since 1999 and has been successful on each tendering exercise since that date.
- 2.3 It is proposed to dispose of the previous winter facility to gain a capital receipt for the Council.
- 2.4 Upon completion of the contract, the Council will be able to consider bringing the service in-house, or retendering the contract. Either way the existing cost implications of having to pay for the facility will no longer be a requirement as the Council will own its own facility. Any subsequent retender will only have the requirement of supply of gritting vehicles and drivers which will dramatically reduce the costs to the Council.

3.0 Cost Implications

- 3.1 *Headline Financial Analysis* - the capital cost is £2.6m. This will be funded from Public Works Loan Board borrowing. The period of borrowing will be linked to the useful life of the asset, 25 years, resulting in annual repayments of £146k (based on borrowing rates as at Nov 2019). In addition, there are increased costs of running the new facility, due to its larger footprint, of £44k per annum.

The estimated annual savings are £191k based on the average contract costs over the past 10 years which would therefore cover the borrowing and increased facility costs.

3.2 *Detailed Acquisition Costs* - the contractor has agreed to sell the newly constructed facility to the Council for the sum of £2,500,000. The purchase will also require an additional £132k for acquisition fees, broken down as follows:

- Stamp duty land tax £115,000
- Legal fees £10,000
- Clerk of Works/Surveyors £2,000
- Asset Management fees £5,000

Subject to approval, a supplementary Capital estimate for this proposal is included within the Growth and Strategic Investment Cabinet Report that is also on this agenda. If Cabinet approve the acquisition, this will be reported to Council within the Growth and Strategic Investment Report.

3.3 The contractor has provided a full breakdown of the construction costs of the facility which have been checked and substantiated by Property Services colleagues as follows:

'We would reference the BCIS cost data (based on 4Q 2019) which provides a median unit cost rate of £1,500 per m² for a similar building type and size in this location which results in a provisional cost estimate of about £2.56 million.' This excludes the cost of land purchase which is currently estimated at £350k.

3.4 *Detailed Borrowing Costs* - based on an estimated useful life of the facility of 25 years, over this period the Council would borrow £2.632m. This would result in a repayment per annum of £146k and a total outlay of £3.7m.

3.5 The disposal of the existing depot is expected to generate a capital receipt of £250k and this will be allocated to the Council's Single Capital Pot.

3.6 *Detailed Revenue Savings Assessment* - an analysis has been undertaken of winter gritting operations over the last 10 years. Applying these numbers to the 20% rate saving would indicate potential revenue savings of between £190k and £280k per annum. A risk analysis has also been undertaken.

4.0 Five Case Business Model

4.1 Strategic

The Council needs to plan for the future and take initiatives to reduce future revenue costs. The facility meets the requirements of government statutory guidance and ownership of the facility will place the Council in the best possible position to make strategic decisions on the future procurement and delivery of the service. Purchase of the facility will provide a cost-effective solution for the Council, coupled with ongoing revenue savings and opportunities for the future.

4.2 Economic

The Council needs access to the specified facility. The current contract allows the contractor to recover the cost of the facility through his tendered revenue rates. At

the end of the contract, the Council would have to either retender in the same manner or build its own facility. By purchasing the facility now, the Council will benefit from a 20% reduction in tendered rates for the remainder of the contract which will offset the prudential borrowing payments and additional running costs. The proposal offers the Council excellent value for money now, with the opportunity for continuing revenue savings for the future. In addition, should the Council decide to retender the contract at the end of the current contract, it can do so based on ownership of the facility. This will generate a substantially lower tender value which would only require the provision of vehicles and drivers.

4.3 **Commercial**

Purchase of the facility will allow the Council, should it wish to, the option to utilise the facility for its own use. This could include bringing the service back in house at the end of the contract, rather than retender it, and also potentially offer the use of the facility to other Liverpool City Region Combined Authority member authorities. The facility has been offered to the Council for a purchase price of £2.5m (with an additional cost to the Council of £132k in acquisition fees) in return the Council will grant the 4-year contract extension now, and the contractor will reduce his tendered rates by 20% for the remainder of the contract, subject to existing contract price fluctuation clauses.

4.4 **Financial**

The cost to purchase the facility is £2.62m funded through prudential borrowing. Professional property colleagues have confirmed that should the Council decide to build its own facility at the end of the contract, the cost at 2019 rates would be £2.56m plus the cost of land purchase (likely to be at least £350k). Furthermore, this option for the Council to build its own facility would not generate the 20% revenue saving which is estimated to be between £191k and £280k per annum over the remainder of the contract.

4.4.1 *Savings on Maintenance and Running Costs on the Existing Depot*

The existing Depot, which is recommended for disposal attracts the following annual expenditure:

- Water rates - £500.00
- Business rates - £3,400.00
- Electricity costs – £1,000.00
- Maintenance - £5,000.00 (average)

- **Total existing annual expenditure £9,900.00** (These costs are currently funded from the existing revenue budget for Winter Service)

4.4.2 *Additional Maintenance and Running Costs of the New Facility*

Purchase of the new winter facility will attract the following costs (which will be offset by the disposal of the existing depot)

- Business rates - £44,140 (This assumes a rateable value of £90,000 and a non-domestic rating multiplier of £0.491)
- Maintenance and Utilities – £10,000 (This is based on the existing maintenance and utilities for the existing facility, factored up due to the larger footprint)

- **Total annual expenditure £54,140** (these costs will be funded from the existing revenue budget for Winter Service)

4.4.3 Financial Summary

Costs

£2,500,000	Acquisition Cost (Land & Building) (One Off)
£132,000	Acquisition Fees (One Off)
£54,140	Estimated New Facility Maintenance / Premises Costs (Per Annum)

Benefits

£250,000	Capital Receipt from Sale of Existing Site (One Off) (subject to Cabinet decision)
£350,000	Estimated Residual Land Value
£190,861	Estimated 20% Annual Contract Saving (Based on 10 Year Actual)
£9,900	Existing Facility Premises Costs (Per Annum)

4.4.4 Options Appraisal

The Net Present Value (NPV) appraisal technique has been used to assess the financial viability of both the recommended option to purchase the facility and the option for the Council to build a facility on a new site. NPV represents the return / gain on initial investment in present day terms in line with the Treasury Green Book appraisal methodology using a standard discount factor of 3.5%. A positive NPV indicates that a project is worth undertaking from a financial point of view. The output from the appraisal has been captured in the table below.

Options	Option Description	NPV	IRR	Payback (Yrs.)	Discounted Payback
1	Purchase (Recommended Option)	£182,634	4.15%	16.25	24.13
2	Council Build	-£249,596	2.72%	19.19	No Payback

The recommended option results in a positive NPV of £0.18m indicating that the project is worth undertaking from a financial point of view. This represents a gain of 7.31% on the initial purchase price investment of £2.5m.

The Council build option produces a negative NPV which indicates that this would not be worth undertaking from a financial point of view.

4.4.5 Sensitivity Analysis

This financial appraisal also considers sensitivity analysis to assess the impact of changes to key assumptions in the business case. The key points from the sensitivity analysis are:

- **Annual Contract Savings** – Annual contract savings have been calculated at 20% of the average cost for the last 10 years. These are assumed at £190,861 per annum. These would need to fall to £179,780 per annum to produce a negative NPV (a reduction of 5.8%). However, given the saving is based on the overall contract spend, then if the contract saving were to reduce, for example

due to improved weather conditions in any year, then this would be fully offset by the overall reduction in cost.

- **New Facility Premises Costs** – The annual premises costs have been estimated at £54k and the higher cost compared to the current facility (£9.9k per annum) is due to the increased footprint and the prudent approach taken to cost estimation. These costs would need to increase by over 20% to produce a negative NPV. Ongoing revenue costs such as these would be fully reviewed and understood prior to the purchase.
- **Acquisition Fees** – Acquisition fees would need to increase from 5.3% to 13% i.e. from £132k to £315k to produce a negative NPV for the proposal. Fees will be formalised and understood prior to purchase to ensure that fees do not escalate above this point.

The detailed sensitivity analysis is as follows:

Sensitivity Group	Sensitivity Description	Projected Net Present Value (NPV)	% Discounted Return / (-Loss) on Initial Investment
		£000s	%
Recommended Option (25 Year Analysis)		183	7.31%
Contract Saving Sensitivities	Annual Contract Saving Based on Actual Costs Incurred in the Last 10 Years Less 10%	(132)	-5.28%
	Annual Contract Saving Based on Worst Year in the Last 10 Years	1,599	63.95%
New Facility Premises Cost Sensitivities	Premises Costs Increased by 10%	93	3.74%
	Premises Costs Increased by 20% [Breakeven]	0	0.00%
	Premises Costs Increased by 30%	(85)	-3.40%
Acquisition Fee Sensitivities	Acquisition Fees Increased from 5.3% to 7%	140	5.59%
	Acquisition Fees Increased from 5.3% to 13% [Breakeven]	0	0.00%
	Acquisition Fees Increased from 5.3% to 20%	(185)	-7.41%

4.5 Management

Ownership of the facility will allow the Council to manage and control this significant asset, controlling its use, both for the existing contract but more importantly for future service delivery and opportunity. The Council will manage the facility and the contractor will have indemnity insurance and be liable for any damage caused in the delivery of the service. This has been the case historically when utilising the existing depot at Damfield lane.