

## **Attachment 8**



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## 7 Public Excluded Agenda – 25 August 2004

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### p107 7.1 Mangawhai EcoCare Project Documentation

**Chief Executive**                      **File 4505.01**

A report by the Chief Executive, and its associated papers, are attached.

Since commencing this project in 1998 Council has undertaken a comprehensive and exhaustive consultation process that has seen a very high level of acceptance of the need for a community wastewater scheme in Mangawhai.

The key drivers for the project are the protection of the harbour, affordability and protection of community health.

Following the acceptance of Simon as the preferred proponent there has been a robust and strenuous negotiation of the contract document. This has now been completed and the original costs to the users as advertised in the Statement of Proposal can be achieved.

#### **Recommended**

*That the contract documentation as drafted and agreed between Simon Engineering and Kaipara District Council be executed and the Mangawhai EcoCare project proceed.*

#### **Reason for the recommendation**

The contract documentation reflects the principles adopted by Council for the EcoCare Project and the needs of the community for an affordable and effective wastewater scheme that will deliver both health and environmental benefits to standards that are acceptable to both the community and the regulators.

#### **Recommended**

*That Council resumes in open meeting.*

**Public Excluded Item**

**File Number:** 4505.01  
**Report To:** Council  
**Meeting Date:** 25 August 2004  
**From:** Chief Executive  
**Subject:** Mangawhai EcoCare Project Documentation  
**Date of Report:** 11 August 2004  
**Signed By:**

**Public Excluded**  
\_\_\_\_\_  
Jack McKerchar**Conclusion**

Since commencing this project in 1998 Council has undertaken a comprehensive and exhaustive consultation process that has seen a very high level of acceptance of the need for a community wastewater scheme in Mangawhai.

The key drivers for the project are the protection of the harbour, affordability and protection of community health.

Following the acceptance of Simon as the preferred proponent there has been a robust and strenuous negotiation of the contract document. This has now been completed and the original costs to the users as advertised in the Statement of Proposal can be achieved. These charges are: -

Annual charge (indexed to the rate of inflation)	\$ 483.75
Existing Start-up Fee	\$ 1,450.00
New Properties Start-up Fee	\$16,312.50

The costs of the project have risen as follows: -

- Construction Cost \$15.6m to \$16.1m
- Fees and interest \$1.9m to \$2.9m

These are conservative figures and as can be seen in the body of the report it is likely that savings will be made on these. At this time no decisions have been made on the use of the subsidy. A key unknown for this project is the final disposal site. This will be determined once the contract is signed.

Once the contract is signed the resource consenting process can commence and details of the physical construction process determined. When this is done a full report to Council on final costs and use of the subsidy money will be tabled for consideration and decision.

**Recommendation**

*That the contract documentation as drafted and agreed between Simon Engineering and Kaipara District Council be executed and the Mangawhai EcoCare project proceed.*

**Reason for the recommendation**

The contract documentation reflects the principles adopted by Council for the EcoCare Project and the needs of the community for an affordable and effective wastewater scheme that will deliver both health and environmental benefits to standards that are acceptable to both the community and the regulators.

**Background**

This project had its genesis in the 1980s when proposals were put to the community in 1981 and 1988 to provide a community sewage scheme for Mangawhai. These proposals were reject and the matter was held in abeyance until 1998 when the Council commenced its Infrastructural Assets Study which lead to the development of this project. In the meantime water quality sampling showed increasing pollution of the Mangawhai harbour.

Council worked closely with the community and received support from the community for the proposal that the harbour must be protected along with the community's health. This was followed by a comprehensive consultation and information process that involved amongst other instruments, public meetings, a community liaison group, open days, newsletters and newspaper articles.

Council advertised for registration of interest and then short listed proponents. A final selection was made and Simon Engineering was awarded preferred proponent status. Their bid was \$4.3M (Net Present Value) below the next closest and they had the advantage of a financial model that enables cash flows to be smoothed to provide the greatest benefit to the community.

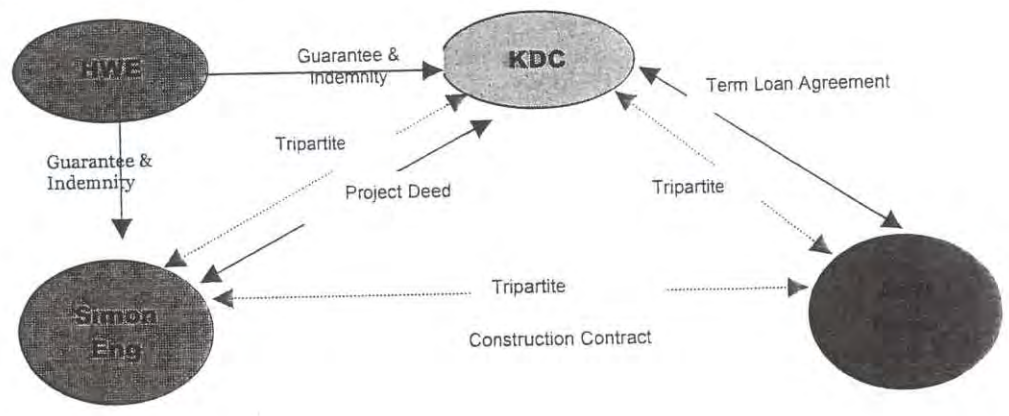
This resulted in Council adopting the following charging regime for ratepayers: -

Annual charge (indexed to the rate of inflation)	\$ 483.75
Existing Start-up Fee	\$ 1,450.00
New Properties Start-up Fee	\$16,312.50

Council also received confirmation that it had been successful in obtaining government subsidy of \$6.63M for the project.

**Contract Framework and Negotiation**

Outlined below is a graphical representation of the contractual structure and the documents and links involved: -



**Reason for the recommendation**

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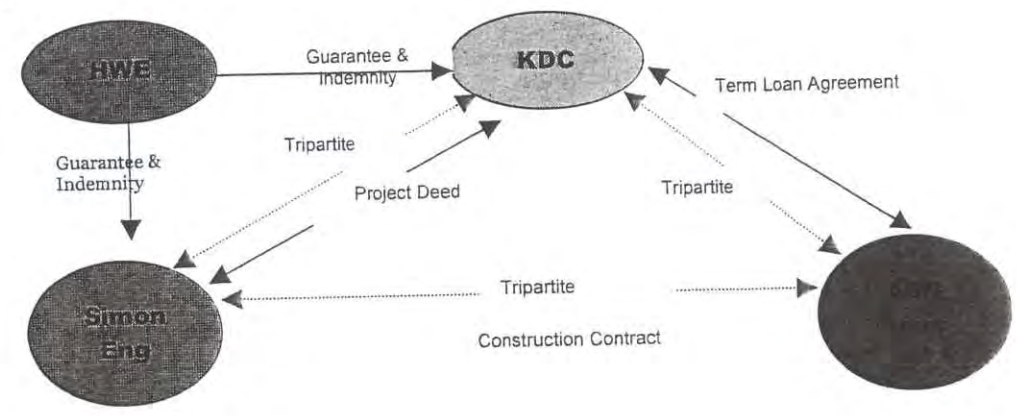
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**Contract Framework and Negotiation**

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**Mangawhai Ecocare Project Legal Structure**

- 1 **Project Deed.** The key document that provides for design, construction and operation of the Facilities and the provision of required services. Provides for payments to SEA of the operating toll when Commercial Acceptance is achieved, Council owns the Facilities and the services are fully provided.
- 2 **Term Loan Agreement.** The key financial document that provides that Council is obligated to finance and purchase the system from ABN provided that Commercial Acceptance is achieved. Five year fixed interest rate term with ABN having first option to refinance if Council desires.
- 3 **Guarantee and Indemnity.** Is the prime legal document that ensures that Council is protected from extra costs if the project does not achieve Commercial Acceptance, or if SEA defaults in the delivery of Services during the 10 year operating period. The Guarantee and Indemnity is provided by Henry Walker Eltin (The parent company of Simon Engineering) provides security to Council that it will meet all of SEA obligations under the Project Deed (including defaults, termination or similar issues) and cover Council's costs if SEA fail to do so. Calling of the guarantee would be a "last resort" legal option.
- 4 **Construction Contract:** Is the contract between ABN and the SEA that provides for the development of the Facilities. Council is not a party to this contract.
- 5 **Tripartite Agreement:** Is the agreement signed by Council, SEA and ABN that outlines the relationships between the parties relevant to the:
  - Right of ABN to step in and remedy default by SEA during the Construction Period,
  - Transfer of ownership of the assets from SEA to ABN progressively as they are constructed
  - Rights and obligations on early termination of the Deed; and
  - Sale agreement between ABN and Council for purchase of the Facilities on completion (ie: at Commercial Acceptance).

Key features of the contract as negotiated are: -

<b>Financial</b>	
• Guaranteed maximum construction price	\$16.1 m
• Maximum fees (Council, abn amro, interest)	\$ 2.9 m
<b>Total</b>	<b>\$19.0 m</b>
• Operating toll year 1	\$0.56 m
<b>Timing</b>	
• Achieve consents	6-12 months
• Development and construction period	Up to 14 months
• Commissioning and proving tests	3 months
• Commercial acceptance/ services commence	Day one

<b>Loan period</b>	
• From commercial acceptance	Five years
• Interest rate	Fixed
• Option	ABN has 1 <sup>st</sup> option to refinance.

Through these negotiations there has been some further price increases negotiated to enable the contract to be finalised and to lock in further price certainty for the capital costs of the facilities provided a resource consent is achieved by March 2005. This was an important issue during the negotiations as price increases in materials and increased labour costs driven by demand in the building construction sector has been significant over the last 12 months. In addition official interest rates have increased four times this year to now be at 6%.

This is now an effective maximum based on the current scope with savings in interest 100% to Council's benefit and the GMP providing a mechanism to share any construction savings equally with SEA. Reductions in the GMP will also flow through to lower fees and interest charges. In addition, although not included at this stage, as it would further complicate the negotiation process, consideration will be given after signing to negotiating a share in construction interest savings with SEA in order to provide an incentive to complete construction in the shortest possible time and therefore make further savings in interest charges to Council.

**Project Budget and Finance**

The negotiations referred to above have resulted in some increased costs in both the construction and the fees and charges in the project. A key has been to get early payment of Council's initial costs. The table below compares the current situation with the situation reported to Council in February 2004: -

	Feb 04 \$ms	Final \$ms
Capital Expenditure	15.6	16.1
KDC Fees, Other Fees and Interest	1.9	2.9
<b>Project costs</b>	<b>17.5</b>	<b>19.0</b>
<b>Year one operating costs</b>	<b>0.56</b>	<b>0.56</b>

The key items to note are the operating costs are unchanged and the levels of rates and connection charges as included within the Statement of Proposal can be maintained as the above is seen as a conservative position to ensure sufficient funding is available within the debt facility established by ABN Amro to manage all circumstances including potential to amend the final disposal site, increased treatment standards, additional reuse, and or additional capacity to meet recent demand increases. If this level of debt is not required then maximum interest and fees will be reduced.

None of these figures allow for the subsidy that has been granted.

### **Sanitary Works Subsidy Scheme**

We have been successful in obtaining subsidy of \$6.63M (exclusive of GST) to assist with the funding of this project. No decision has been made on the use of the subsidy. There are a number of issues to be resolved once the contract with Simons is signed. This includes the final disposal site and the resource consenting process. Also we will have to review the project management regime for the project to ensure we have a structure that will deliver to the community in a timely and effective way.

Council has considered the subsidy being used for the physical connection to each property and providing some reduction in annual costs to the users.

Once the contract is signed and the project has some certainty as to process a full report on the use of the subsidy will be brought to Council for consideration and decision.

### **Rights and Obligations of the Parties**

The rights and obligations of each of the parties are spelt out within the documents that incorporate the risk transfer approach as adopted by Council. The major change to the original Risk Matrix is due to the change from a BOOT to a DBFO methodology as discussed previously. This has created a changed relationships between firstly the Promoter (SEA) and the Financier (ABN) and secondly between Council and the ABN.

The primary changes means that as Council will now be the owner of the assets as from Commercial Acceptance they will now have to have a greater role in monitoring regulatory changes, changes in treatment standards and all proposed reuse arrangements. Council will now also have to take insurance coverage on the facilities as from Commercial Acceptance.

The other key change is that the role of the financier is now more explicit than originally contemplated within the Risk Matrix and therefore a separate Term Loan Agreement is required between Council and the Financier. The interest rate charges and bank fees were previously all included within the overall monthly toll payments and were not visible to Council. Now that a separate agreement is required these fees and charges are visible to Council and have been set in accordance with Council's decision in August 2003 namely a fixed five-year interest rate loan.

Attached is a summary table that outlines how these risks have been allocated and provides a cross reference to the relevant clauses and schedules.





RISK ISSUE	RISK ALLOCATED TO		DEED REFERENCE	COMMENTS
	KDC	PROMOTER		
<b>PLANNING</b>				
Construction, Consents and Rulings <ul style="list-style-type: none"> <li>• Tax</li> <li>• Planning</li> <li>• Consents</li> </ul>	<ul style="list-style-type: none"> <li>✓</li> <li>✓</li> <li>✓</li> </ul>	<ul style="list-style-type: none"> <li>✓</li> <li>✓</li> <li>✓</li> </ul>	N/A 20 2	No taxation specific issues with each party responsible for own GST. Development obligations include all authorisations. Promoter has obligation to achieve all Consents as well Land Disposal or Reuse Agreements. Council must work with Promoter to achieve consents and assist in finding a suitable land disposal option.
<b>DESIGN AND CONSTRUCTION RISK</b>				
Specification and capacity of Facilities	✓		20 & 21	Must design and develop facilities in accordance with the Deed and Project Plan. Clause 28 enables Council to control any Modifications and hence any changes in price. Project Plan includes outline of technical approach and minimum commissioning tests. Project Director Endorses drawings etc but does not accept design risk.
Design and Construction of Facilities	✓			
Construction Cost Over Runs <ul style="list-style-type: none"> <li>• Caused by Kaipara District Council</li> <li>• Caused by Contractor</li> <li>• Force Majeure</li> </ul>	✓		34  16 & 28	Delay costs payable if council causes delay, maximum daily amount subject to proof of actual costs. Council also not to interfere or delay in responding to any requests. GMP process through Schedule P and clause 16 controls costs to Council. Clause 28 controls any Modifications. FM events are defined protects the promoter from unlimited exposure all others at SEA risk.
Construction Timing		✓	29, 34	Limited scope for extension of time but not past Sunset Date, delay costs payable if Council causes delays. Council does not pay toll until Commercial Acceptance (CA) achieved, hence there are commercial drivers on promoter to complete on time.

RISK ISSUE	RISK ALLOCATED TO		DEED REFERENCE	COMMENTS
	KDG	PROMOTER		
Industrial Relations		✓	1.1, 16, 19	Promoter can get time extension if IR action is specifically targeted at Council or the Project otherwise to Promoter's cost and risk.
Continuation of Services during Construction		✓	20.3	Must maintain any services currently being provided.
Load and Volumes		✓	3, 20,	Promoter must provide the Services to the Standards and develop the Facilities to accept all load and volume up to the level nominated within the Project Plan. Council to order a Modification if additional capacity is required. Key Issue is Council agreed to lower capacity in exchange for lower construction costs during tender evaluation phase.
<b>COMMISSIONING, OPERATING &amp; MAINTENANCE RISK</b>				
Commissioning of new plants		✓	30 & Sch. A.	Must be achieved as a condition for Commercial Acceptance (CA). Promoter does not get paid operating toll until CA is achieved.
Operations of Plants		✓	3	Must provide Services to defined standards once CA is achieved. Toll to be reduced if standards not achieved.
Service Performance		✓	3, 18 & Sch. C	Toll reductions if Services not to standard.
Occupational Health and Safety		✓	22.6	Promoter must submit and implement a Health and Safety Plan that complies with all regulations.
Illegal discharges and connections		✓	4	Promoter obliged to monitor, identify and report to Council. Council to pursue remedies and pay Promoter any fines subsequently levied less any Council costs.
<ul style="list-style-type: none"> <li>• Identification</li> <li>• Pursuit of legal remedies/ damages</li> </ul>	✓			
Outflow characteristics and achievement of estuary standards		✓	1.1 & Sch. A	Promoter to monitor and report environmental conditions of the estuary as well as monitoring outflow of the plant as well as qualitative monitoring program. Must also comply with all consents.

RISK ISSUE	RISK ALLOCATED TO		DEED REFERENCE	COMMENTS
	KDC	PROMOTER		
<b>COMMERCIAL TERMS</b>				
Proponents' Bid Costs		✓	2	No allowance for reimbursement of bid costs if Project does not commence due to non achievement of consent or early termination.
Inflation/ Foreign Exchange and or Interest Rate Movements	✓ (Change)	✓	1.1 & Sch	Price has now been fixed with a defined escalation clause to apply to contract price if Consents not achieved within 6 months. Toll has defined inflation method all cost increases to Promoter account. ABN will fix interest rate on Commencement Date.
Insurance	✓ (Change)	✓	Sch. R	Promoter insures plant up to CA, Council now insures post CA because it owns the assets.
Taxation		✓	17	No taxation specific issues with each party responsible for own GST.
Finance Availability/ Structure		✓	Recitals Tripartite	ABN will finance the project now under a DBFO structure instead of the previous BOOT arrangement.
Provision of Securities		✓	N/A	Commercial Acceptance regime plus Default process protects Council as does the Guarantee and Indemnity from HWE.
Assignment/ Novation		✓	25	Council rights to approve any novation Promoter responsibility
Corporate Structure		✓	5	Defines limited scope where promoter accepts some risks and Council others. Defined process to mitigate costs. This has been a negotiation issue through the process with some concessions being granted if standards are changed.
Changes in Law	✓ (Change)			Asset Condition reports required each 5 years, Council assumes ownership once CA occurs and gets option to purchase if Council terminates due to default by the Promoter. If they don't want them ABN is left as owner and they recover costs from HWE.
Transfer of Facilities on Completion		✓	6.6 30, 36, 40	
• Asset Condition		✓		
• Residual Value		✓		

RISK ISSUE	RISK ALLOCATED TO		DEED REFERENCE	COMMENTS
	KDC	PROMOTER		
				Council must only pay cost to complete less all Council costs if they want to purchase assets not complete. ABN also can step in to complete facilities and then sell to Council.
<b>REGULATORY ISSUES</b>				
Obtain and retain Consents		✓	2 & Sch. C	Promoter has obligation to achieve all Consents as well Land Disposal or Reuse Agreements. Council to cooperate and assist.
Monitor NRC rulings and meet increased Licence Standards	✓ (Change)	✓	5	Primary responsibility rests with Promoter but Council has some responsibility under defined Changes in Law and as they are now the asset owner.
Monitor and address changes in regulatory regime	✓ (Change)	✓	5	Primary responsibility rests with Promoter but Council has some responsibility under defined Changes in Law.
<b>SITE ISSUES</b>				
Kaipara District Council Sites				
<ul style="list-style-type: none"> <li>• Environmental Report</li> <li>• Site Availability</li> <li>• Contamination</li> <li>• Archaeological/ Heritage</li> <li>• Iwi agreement</li> </ul>	<ul style="list-style-type: none"> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> </ul>	<ul style="list-style-type: none"> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> </ul>	55 9, 10	<p>Cost of initial report shared equally. If Council land Council pays to remedy. Promoter pays all environmental issues. Council to make Mangawhai Park available.</p> <p>If iwi site issues or artefacts are found Promoter gets time but not costs. Council to authorise Promoter to enter land.</p>
Other Sites				
<ul style="list-style-type: none"> <li>• Environmental Report</li> <li>• Site Availability</li> <li>• Contamination</li> <li>• Archaeological/ Heritage</li> <li>• Iwi Agreement</li> </ul>	<ul style="list-style-type: none"> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> </ul>	<ul style="list-style-type: none"> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> <li>✓</li> </ul>		<p>If iwi site issues or artefacts are found Promoter gets time but not costs. Council to authorise Promoter to enter land. Promoter takes all other risks.</p>

RISK ISSUE	RISK ALLOCATED TO		DEED REFERENCE	COMMENTS
	KDC	PROMOTER		
CUSTOMER INTERFACE ISSUES				
Community Liaison	✓	✓	3.7	Council retains prime responsibility but Promoter must cooperate including attending any CLG meetings and responding to customer issues. Council will need to proactively manage ratepayer issues during the construction period and liaise between Promoter, Council and the ratepayers. Recommend Council look at someone on a 50-100% commitment during planning and construction period to facilitate smooth implementation.
Manage customer interface including billing and accounts	✓			Not mentioned Council responsibility.
Public Health		✓	53.1	Specifically covered in the indemnities. Promoter assumes public health risk. Introduction of a toxic substance to the system by a third party is a Force Majeure Event.
All other risks		✓	57	

Whilst the risk matrix outlines the risk allocation Council assumes clear responsibilities as the client to work cooperatively with the Promoter and to act reasonably and not unduly delay or frustrate the process. This includes not interfering on site or delaying decisions.

To this end a Contract Management Manual will be prepared outlining the rights, obligations and contractual expectations of each party to ensure there are no misunderstandings or uncertainty with responsibilities or process.