



MUNICIPAL WASTE PERFORMANCE CONTRACTS



A REPORT BY EUNOMIA FOR ACR+ AND THE EUROPEAN ENVIRONMENTAL BUREAU

APPROACH

This report focuses on an economic tool which can improve waste management, in line with the European waste treatment hierarchy, and encourage the move to a circular economy model – waste performance contracts. The report proposes the following definition for performance contracting:

'a contract for the management of waste which, through the action of a contractually agreed payment mechanism related to defined performance indicators and targets, incentivises the movement of waste management further up the waste hierarchy, and enhances the prospects for improved resource efficiency and the flourishing of a circular economy.'



REPORT

- To identify the technical and financial structure of performance contracting for waste management;
- To identify the potential administrative basis, legal basis and governance of these performance contracts;
- To identify the necessary conditions for such contracts to be established, including an exposition of challenges and solutions for implementation.
- To provide examples of the possible application of performance contracts and simulate what they could look like.



SCOPE OF PERFORMANCE CONTRACTS

The variety of approaches to waste management contracting across the EU makes it difficult to describe how performance contracts should be designed. Contractors may have responsibility for different parts of the overall waste management system. The report therefore considers a range of 'contract scopes' which reflect the prevailing practice.

Contract scopes considered include:

- Communications;
- Re-use and preparation for re-use;
- Waste collection (including conventional household collections, collection of non-household waste, container parks / civic amenity sites, bulky waste collections and street sweepings);
- Waste treatment;
- Integrated contracts.



KEY CHARACTERISTICS OF WASTE MANAGEMENT CONTRACTS

There is a common set of characteristics which need to be considered when drawing up a waste performance contract. These include:

- **Degree of control:** The factors influencing the performance measure have to be within the contract scope.
- **Application:** It is important for municipalities to apply a 'reasonableness' test before incorporating performance-related payment mechanisms into contracts and are suitably confident that they are legally enforceable. Certain factors need to be assessed including whether there is political or community acceptance of the improvement measures required by the contract, whether there is compliance with public procurement rules and laws, and whether there is the possibility to apply contractual default payments depending on achievements. It is important for municipalities to apply a practicality test before incorporating performance-related payment mechanisms into contracts. Municipalities must be confident that such mechanisms are legally enforceable.
- **Measuring performance:** Performance can be measured in two different ways -
 - By measuring outcomes i.e. the extent to which the waste hierarchy is respected or through other environmental indicators e.g. energy use, greenhouse gas emissions, air quality etc.
 - By using measures that more traditionally relate to questions of service 'quality'
- **Performance indicators:**
 - The indicator should reflect a genuine improvement in environmental, or other, outcomes;
 - The indicator should be chosen to reflect the actions of the contractor and not include external factors; and
 - The performance measure is ideally specified in terms of a change relative to a baseline.
- **Performance incentives:** Incentives should be used only where they:
 - Incentivise the application of the waste hierarchy in the scope of the contract;
 - Are in line with the degree of control that the contractor can reasonably be expected to have over the contracts outputs related to those indicators; and
 - Avoid the risk of 'double counting', rewarding or penalising the contractor twice for the same outputs.
- **Geographical considerations:** The geographical scope of a waste management contract should ideally reflect the economically optimum scale for the infrastructure or logistics to provide the services being contracted for. It generally makes sense to benefit from economies of scale, subject to the costs of haulage becoming excessive.
- **Duration:** In drawing up a contract, the following considerations are worthy of note:
 - providing stability versus having the flexibility to adjust incentive schedules
 - lifespan of the infrastructure and equipment needed to deliver the services
 - incentive profiling over time which may affect how providers are able to meet contract conditions
 - whether flexibility should be built into the performance contract to account for reviews of objectives
 - considering the impact of potential legislative or regulatory changes over the duration of the contract that may impact performance levels
- **Governance considerations:** Governance structure of performance management contracts will largely depend on the relationship between the contracting parties. For example, where the client and the provider are part of the same organisation, a service entity and a client entity would be needed to provide the structure necessary for contract-like elements to be implemented.
- **Relationship with other economic instruments:** Performance contracts do not operate in isolation from the wider regulatory and fiscal environment in operation. It is important therefore for municipalities to consider how proposed performance contracts would operate in relation to wider economic considerations, such as countries where landfill costs are low or because of the presence of a Pay-as-you-throw or Extended Producer Responsibility schemes.



EXAMPLE : PAYMENT FOR AVOIDED TONNAGE OF RESIDUAL WASTE TREATMENT

An example is presented below where, for an increasing tonnage of avoided disposal over time, the contractor receives an increasing proportion of the financial savings made by the municipality. There may be good reasons to have a schedule of increasing marginal bonuses which recognise that a contractor is likely to seek the lowest cost wins first, and the more expensive ones later.

Example of avoided disposal incentive payments



Note: All of the indicators would require a well-specified baseline and regular and robust data monitoring in order to be effective. This baseline could be set by the contracting authority, in which case, it seems desirable that these should be included within the contract specification(s) quoted during the procurement process, or developed in conjunction with the contractor, for example, following an initial period of monitoring (e.g. the first contract year).



RECOMMENDATIONS

There are key considerations emerging from this report:

- ✓ The aim of moving a larger proportion of waste to be managed at higher levels of the hierarchy is best achieved through the effective application of performance incentives at the collection end of the waste management system;
- ✓ Performance contracts that cover door-to-door collection where there is a good recycling and biowaste collection scheme in place, and those that also cover bulky waste collection and provision of CA sites, can have a more positive effect than on-road communal containers or container parks;
- ✓ The wider the scope of the contract (i.e. the more waste streams and collection methods in the scope), and the wider span of control over outputs that the contractor has, the better chance a municipality has in applying 'whole system' performance requirements;
- ✓ The scope of the contract and the scope of the performance mechanism, in basic terms, must match up, reflecting how the market works (i.e. the scope of each entity/contractor's services) in different countries.;
- ✓ Municipalities should consider which performance indicators to include in contracts carefully and keep them to a few key measures that are predicted to have the most positive effect;
- ✓ The performance measure is ideally specified in terms of a change relative to a baseline (which can be linked to a projection if needs be);
- ✓ As well as financial incentives, others might relate to matters that are not purely financial. As such, environmentally minded municipalities could consider setting incentives related to greenhouse gas savings, and a reputable measure of the external benefits which may accrue to society.
- ✓ Ideally performance contracts should include a mechanism that is designed as far as is possible to normalise outputs to take account of these other factors (e.g. economic performance) that will have a bearing on consumption and the related generation of waste; for example, indexation related to an appropriate economic indicator such as GDP or per capita disposable income or expenditure,.

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