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Mr Jim Kells,  
Chairman,  
Irish Waste Management Association,  
84-86 Lower Baggot Street,  
Dublin 2.

23<sup>rd</sup> March 2012

Dear Jim,

Re: **DKM Review of Transitional Costs of Changing Market Structure**

Further to recent e-mail correspondence and my meeting with the committee on 9<sup>th</sup> March, I set out below a brief estimate of the order of magnitude we believe might apply in terms of the transitional costs for the Irish economy (and thus for consumers and taxpayers) of a transition from the current market structure (competition in the market) to the proposed alternative structure (competition for the market).

A number of significant one-off and recurring costs will arise if the market structure is altered as proposed, and we deal with each of them below.

### **Replacement of bins**

In moving from a situation of several firms supplying the market to a single supplier servicing each county, the first and most obvious cost is in respect of procuring and delivering new bins, and collection of old bins.

We base our estimate of the following:

- As of 2011, we estimate that there are 1.45 million single unit households in the State.
- A set of three wheelie bins costs approximately €66 (€22 each).
- There would also be a cost for delivery of the bins to households and collection of old bins. We add a cost of €25 per affected household for this.

- Our recent survey reported average market share of respondents of 35%; we assume that this would apply to successful tenderers, and thus 65% of households would have to have their bins replaced on the award of the tender.

On this basis, the initial cost of new bins would be approximately **€86 million**.

There is in addition the potential for further costs under this heading when contracts are re-awarded. We believe incumbents would have a strong advantage in such retenderings; however, if there was a turnover of say one-third at retendering then recurring costs would be in the region of **€30 million**.

It can be argued that, once tender awards are announced, the unsuccessful tenders will simply sell their bins to the successful tenderers. While this would avoid the collection and delivery costs, it would not avoid the actual bin costs themselves which will remain a cost for the successful tenderer, and must ultimately be recovered from consumers. Differing technologies and specifications may also make different firms' bins non-compatible, especially as services evolve over time.

## **Designing, running and enforcing the tendering process**

### ***Costs to the Exchequer***

In the first instance, this will represent a major cost to the public sector. Public procurement procedures are complex and demanding, but the current process could be exceptionally complex, time consuming and expensive, for a number of reasons, including:

- the large number of tenders – in the region of 30 (assuming 27 county contracts including North and South Tipperary, and four separate contracts for Dublin);
- the variability in individual circumstances applying to each; and
- the large range of cost and quality criteria.

This will especially be the case the first time these contracts are brought to tender, but significant costs will recur at each retendering.

Given the combination of central Government costs, local Government costs, and the costs of various advisors, over the design, bid assessment, interview, award, implementation and enforcement phases, a cost of €2-3 million per tender does not appear unreasonable. This equates to an aggregate cost of approximately **€75 million**.

Further costs could arise from potentially defending the process from legal challenge, which must be considered a real possibility given the number a complexity of tenders and the market issues involved. Again, this would be a greater risk in the first round of tenders.

### ***Costs to Bidders***

Tendering for public sector contracts is a significant cost for Irish business – both the successful and unsuccessful bidders. These tenders will be extremely complex by their nature. For the larger counties there is likely to be a high degree of interest, both from Ireland and overseas (we ignore the latter as we are only concerned here with costs for Irish businesses).

If the eight largest tenders (four in Dublin plus Cork, Limerick, Galway and Waterford) each attracts fifteen Irish bids and the remaining 22 tenders each attracts ten bids (local operators must bid to have a hope of staying in business, plus all the large firms are likely to bid for each county in order to maintain their scale and feed their other infrastructure) that makes 340 bids – let us say 350 bids for sake of argument. If each bid costs each bidder €75,000 (staff time plus a range of legal, technical and accounting/tax advice), then the total cost would be **€26 million**. Larger firms might be expected to spend more than this per bid (notwithstanding economics of scale), but smaller firms would likely spend somewhat less.

Costs would likely be somewhat less for subsequent tendering rounds, as international experience indicates a concentration in the sector under circumstances of tendering for the market, so we could assume a figure of **€15 million**.

It should be noted that tendering will be particularly burdensome for smaller firms, and indeed runs the risk of effectively excluding firms which are active in the market now, but are not of a sufficient scale to provide a service to an entire county, particularly if additional requirements (e.g. waivers) are added to the contract conditions. There are numerous surveys in the public domain indicating that the cost of public procurement processes is a barrier to SMEs<sup>1</sup>.

### **Waivers**

It appears that waivers for low income households are to be included in the tendering process. The costs of these will have to be recovered from non-waiver customers.

It is not clear at this stage what the criteria for eligibility for waivers will be. However, data from the Department of Social Protection<sup>2</sup> indicates that in 2010 some 370,000 households received the Fuel Allowance, while a similar numbers received either the Free Electricity or the Free Natural Gas Allowance. Given the deterioration in economic conditions since, a figure of 400,000 household recipients currently would be reasonable.

Let us say the value of the waiver is €150 per annum. On this basis, the cost of waivers, to be recovered from non-waiver customers, would be **€60 million** per annum. We estimate that 15% of households in Ireland live in apartments, so only 85% of this cost would be relevant to the household waste collection service for current purposes. Likewise, 85% of the 400,000 recipients of the waiver (i.e. 340,000) would be relevant for current purposes.

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<sup>1</sup> See for example [http://sfa.ie/Sectors/SFA/SFA.nsf/vPages/Press\\_Centre~sfa-public-procurement-survey-21-05-2010?OpenDocument](http://sfa.ie/Sectors/SFA/SFA.nsf/vPages/Press_Centre~sfa-public-procurement-survey-21-05-2010?OpenDocument)  
<http://www.rte.ie/news/2008/0228/software-business.html>  
<http://www.monaghanlife.ie/index.php/business/10-employment/1891-difficulties-with-government-tendering-process>

<sup>2</sup> Statistical Information On Social Welfare Services 2010, p.100.  
<http://www.welfare.ie/EN/Policy/ResearchSurveysAndStatistics/Documents/2010stats.pdf>

## Household Waste fees Collection

Revenue collection and protection imposes a cost regardless of market structure. Anecdotally, however, it appears that consumers are more willing to pay for services provided by the private sector, who of course have the option of withholding service.

Under the proposed alternative market structure, it appears that the local authorities may take back fee collection responsibilities. This is the norm in Continental Europe where the market structure is similar to that being proposed in Ireland. Whereas in many cases waste management services are contracted out (sometimes to the equivalent of “semi-state” companies), in general the services is funded by the municipalities, who in turn levy and collect the household waste charges.

Evidence in Ireland to date is that the local authorities have a poor record of (i) charging the full cost to householders and (ii) actually collecting the levied charges<sup>3</sup>.

Even if the concessionaire is sub-contracted to collect the money, it may be perceived by the public that they are collecting on behalf of the local authority, and they may be less willing to pay than is the case in the current privatised markets. Under the alternative market structure, also, the concessionaire’s scope to withhold service may be compromised by the concession terms.

If the local authorities are required to establish efficient fee collection systems, that reflect waste collected by type and volume, that will impose significant costs. While it is difficult to be prescriptive, an annual collect cost of 10% of total revenue might be reasonable, which would have to be recovered from householders.

## Other Costs

A number of other costs arise, which we have not been able to quantify, but which will unavoidably be borne either by the taxpayer or the consumer. Among these are:

- Impacts arising from the level of vertical and horizontal integration in the sector, whereby unsuccessful bidders are left with immovable assets whose services no longer have a market. Locally based firms who fail to win local tenders will be particularly vulnerable to this. If larger nationally based firms win the relevant tenders, they will have a preference for using their own infrastructure, leaving the unsuccessful bidders with **stranded assets**. The loss of income streams designed to finance these assets will have a serious impact on these firms (and their banks and other creditors). By the same token, the winning bidders will have to make at least some additional investments in order to service their new markets.
- **TUPE-related costs** may also become an issue, as there is less scope for market pressures to drive costs down, and there may be political pressure for the terms of contracts to include stronger TUPE-related requirements than is the case currently.

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<sup>3</sup> For example, see page 5 of *LOCAL GOVERNMENT AUDIT SERVICE Statutory Audit Report to the Members of South Dublin County Council for the Year Ended 31 December 2009*.  
<http://www.environ.ie/en/Publications/LocalGovernment/AuditService/2009AuditorsReports/FileDownload.27035.en.pdf>

- Other costs (**civil amenity sites, etc.**) may also be included in the tender conditions, which would add further to the price charged to the non-waiver householders.

### Impact on Waste Collection Charges

Eventually, all these costs will be borne by taxpayers or consumers of the service. In the long run, in a competitive environment, the costs of frequent and regular tendering must be recovered from consumers, or firms will not survive. This applies equally to the successful and the unsuccessful tenderers. Likewise in a competitive environment, consumers must ultimately pay for bin replacement, waivers and other costs.

In the table below we set out the potential impacts of the foregoing on the average cost of waste collection per household (assuming that the public sector tendering costs is recovered directly through the tendering process and thus is borne directly by householders).

Based on our previous report, we estimate that the current average charge is €220 per household per annum. There are currently 1.45 million individual unit households in Ireland. Some ad hoc waiver systems are in place at the moment, so let us assume that 5% of households currently do not pay any charge. On this basis the current aggregate cost of the service per annum is just over €300 million (1.45 million x €220 x 95%).

One-off costs are assumed to be recovered over a 5-year concession period (for simplicity finance costs are ignored).

Impact of Change in Market Structure on cost per household				
	Aggregate (€ million)		per Waiver household €	Per non-waiver household €
<b>Annual cost currently</b>	<b>308</b>		<b>70</b>	<b>220</b>
Waiver & non-waiver households (current split)			72,500	1,377,500
Waiver & non-waiver households (new split)			340,000	1,110,000
<b>Impact of:</b>	<b>one-off costs</b>	<b>Annualised costs</b>		
Bin replacement	86	17		
Tendering costs - State	75	15		
Tendering costs - Bidders	26	5		
<b>Sub-total</b>	<b>187</b>	<b>37</b>		
Tariff collection charge (+10%)		35		
cost of waivers		51		
<b>Total additional costs</b>		<b>123</b>		
<b>Grand total costs</b>		<b>431</b>	<b>185</b>	<b>335</b>
<b>%age increase in costs per non-waiver household</b>				<b>52%</b>

As can be seen, these estimates indicate that the transition from the current market structure to the proposed competition for the market structure could potentially add over 50% to the cost of the service per non-waiver household.

This can be considered conservative, given the cost items which we were not in a position to value.

A point worth noting is that the above calculations are on the basis that 100% of households avail of a kerbside collection service. At the moment, this is not the case. It has been argued that costs would be lower if 100% of households did actually avail of a service. If this was the case, then our starting figure of €220 per household would be lower. However, all the additional costs listed (with the exception of local authority collection costs) would be unchanged, and in fact the proportional increase in charge as a result of the change in market structure would be higher. Note that a requirement for all households to avail of a service can be imposed and enforced independently of the market structure.

I trust the above meets your requirements. If you would like to discuss any aspects please give me a call at 6144495 (direct line) or 086 6070190.

Yours Sincerely,

A handwritten signature in black ink, appearing to read 'John Lawlor', with a stylized, cursive script.

John Lawlor.