Bi-annual Indexation
Report Authors: Steve Miles & Neil Thompson

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1 Background and purpose

The following paper introduces and provides the rationale behind a proposed change to the contract indexation, which is considered mutually beneficial to Amey and the authorities.

The paper sets out the current indexation measure before proposing a revised measure and provides a background analysis of the revised measure's impact compared to the contractual mechanism.

2 Current indexation measure

The unit rates paid to Amey, the KPI deductions, and other elements indicated as being "subject to Indexation" are currently modified according to clause 10 of the contract.

Clause 10.1 sets out that the Indexation is calculated

Where Indexation applies, the relevant adjustment shall be applied on April 1st following the Effective Date and on April 1st in each subsequent year (each such date an "adjustment date") and shall be determined by multiplying the relevant amount or sum by the product of:

a. the percentage increase or decrease in each applicable index published for the 12 months ended on the January 31st immediately preceding the relevant adjustment date; and
b. the relevant weighting for that applicable index as set out in the table below:

Indexation Table

	Index	Proportion of costs subject to the index in percentage or as decimal
Labour	Average Weekly Earnings Index (EARN01) as published by the by the Office for National Statistics (ONS)	76.59%
Fuel	Ultra Low Sulphur Diesel (ULSD) contained in the Weekly Road Fuel Prices published by the Department of Energy & Climate Change (DECC)	10.29%
Other	CPI	13.12%

3. Current indexation measure

Given that the January average weekly earnings index is not published until mid-March, the indexation value is unknown until a few weeks before the adjustment date.

In addition, the reliance on fixed rates at a point in time instead of averages means the indexation rate is subject to shocks, such as the Suez Canal blockage, the war in Ukraine, or the impact of lockdown.

The reliance on fixed rates during a period of inflationary shock may mean the authorities are overpaying for the year, or Amey is not recovering their increased costs.
The timing also creates budgetary problems for the authorities as the budget is set using a forecast of Indexation. In the last two financial years, this has resulted in an overspend of £220,000 in 2021/22 and a projected overspend of £375,000 for 2022/23.

3 Proposal

It is proposed that the Indexation moves to a bi-annual calculation based upon averages of the last six months, which would make the indexation value more forecastable and reduce the uncertainty that currently impacts budgets.

A second indexation point protects the authorities and Amey from a fixed indexation that does not reflect current prices.

The proposal is to retain the current mechanisms and weightings but uses average values, with a second adjustment day being introduced.

- April 1st – average values from July 1st to December 31st
- October 1st – average value from January 1st to June 30th

The use of averages should enable Indexation to be a better forecast when it comes to budget setting.

4 Recommendation

It is recommended that members support the amendment of the indexation mechanism and recommend the proposal is taken forward to their next full council.