Agenda Item No: 8

MOBILISING LOCAL ENERGY INVESTMENT – KEY RISKS

To:	**Economy and Environment Committee**
Meeting Date:	**8th July 2014**
From:	**Graham Hughes, Executive Director, Economy Transport and Environment.**
Electoral division(s):	**All**
Forward Plan ref:	**Not applicable** ***Key decision:*** **No**
Purpose:	**To advise members of the increasing risks around the delivery of the Mobilising Local Energy Investment Project (MLEI).**
Recommendation:	**To continue with the MLEI project and review the risk position by December 2014 when there should be greater clarity on:**

a) the timescales to connect to UK Power Network's local network

b) the result of the first auction for financial incentives for solar parks

c) the funding opportunities for energy performance contracting for academy schools

d) the scope for the set up of a Cambridgeshire Energy Company

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1 BACKGROUND

THE NATIONAL PERSPECTIVE

1.1 Government published the Energy Act 2013 to help deliver electricity market reform (EMR) and to attract £110 billion investment to replace current generating capacity, upgrade the grid by 2020, and to cope with the rising demand for electricity. In the UK, a fifth of power stations operating in 2011 will have to close over this decade, and substantial investment is required into energy infrastructure if we are to maintain the secure energy supplies that are critical to our economy. The Coalition Government's vision is:

- **energy security**: to ensure that UK businesses and consumers have secure supplies of energy, for light and power, heat and transport;
- **climate change:** to lead the UK Government's efforts to prevent dangerous climate change and deliver the legally binding targets to cut our emissions by at least 80% by 2050, and to source 15% of our energy from renewable sources by 2020;
- **affordability:** deliver secure, low-carbon energy at least cost to consumers, taxpayers, and the economy as a whole;
- **support growth:** deliver our policies in a way that maximises the benefits to the economy in terms of jobs, growth and investment
- **fairness:** ensure that the costs and benefits of our policies are distributed fairly, so that we protect the most vulnerable and fuel poor households
- to **manage** the UK's energy legacy safely, securely and cost effectively.

1.2 The Energy Act identifies two immediate priorities for UK energy policy: upgrading our energy infrastructure to rebuild our economy, and putting households back in control of their energy bills.

The Cambridgeshire Context

1.3 Cambridgeshire Local Authorities have been working together on the energy agenda since 2008. The Integrated Development Plan (IDP) 2009 identified the energy infrastructure challenge locally and the scale of change required to deliver a 'fit-for purpose' modern energy system with greater independence from fossil fuels.

1.4 More recently the Cambridgeshire Renewables Infrastructure Framework (CRIF) 2012 identified the range of renewable energy technology opportunities, the technical potential of these technologies across Cambridgeshire and the barriers to delivery. It identified that for Cambridgeshire to deliver 28% of its energy needs (for buildings and business, excluding transport) from renewable energy, an investment of £2-6 billion is needed by 2030, of which the public sector could deliver £320 million of infrastructure delivery via schools, non-domestic buildings, land development etc and it could facilitate a further £2 billion of community and commercial projects through a supportive and ambitious policy context.

1.5 Also in 2012, research was undertaken to identify the scale of the energy efficiency market in Cambridgeshire. This identified the market opportunity in Cambridgeshire as approximately £830million across domestic and the non-domestic markets. Green Deal Policy has subsequently facilitated

Cambridgeshire Local Authorities to run a project called 'Action on Energy' to support investment into the domestic market.

1.6 Across the UK, a number of Local Authorities have accessed European Union (EU) funding to develop the skills capacities, finance models and delivery mechanisms to bring forward energy infrastructure at scale. For example, Bristol City Council has set up a Bristol Energy Company, an Energy Services company (ESCO) that is wholly owned by the Local Authority to deliver greater energy efficiency and energy self reliance for its local economy. Other similar examples to Bristol include Birmingham City Council's Birmingham Energy Savers Company and Peterborough City Council's Blue Sky Peterborough Energy Services Company.

1.7 Cambridgeshire County Council and its partners Cambridge City Council, South Cambridgeshire and Huntingdonshire District Council signed a contract with the European Commission's Executive Agency for Small and Medium Enterprise in August 2012, securing a £700,000 grant (75% of the total budget) over three years for financial assistance from the Intelligent Energy Europe (IEE) programme. The aim of the grant is to:

- build capacity and skills (technical, financial and legal) in the local authorities to bring forward investment into energy efficiency and renewable energy generation projects
- set up finance and delivery mechanisms such as a public private energy services company (ESCo) e.g. a Cambridgeshire Energy Company

1.8 For the EU, the set up of a Cambridgeshire Energy Services Company is of interest as Cambridgeshire is a predominantly rural county with two tier local government as opposed to a large metropolitan authority. The learning from the different challenges and barriers to delivery will have wide applicability across Europe.

1.9 A condition of this technical assistance grant money and a demonstration of the new skills and capacities, is that investment into energy projects must be evidenced to at least fifteen times the value of the total grant. For the MLEI Project this means approximately £15million of investment into energy projects must be evidenced by 21st August 2015. If this is not realised then the grant money can be clawed back on a proportional basis according to how much investment has been made, e.g. investment of £5million, a third of the grant is retained.

1.10 The MLEI Project is contracted to:

- Set up a financial mechanism or fund that allows the alignment of private and public sector investment into low carbon energy infrastructure.

- Set up appropriate delivery mechanism(s), e.g an ESCO to deliver low carbon infrastructure projects

- Test the concept of the Fund and Delivery Mechanisms by bringing forward energy infrastructure projects on public sector assets to the value of at least £15 million by August 2015;

2. Project Progress

2.1 Cabinet agreed in October 2013 and January 2014 to set up a Local Authority Fund and borrowing of £15 million from the public works loan board (PWLB) to invest initially into two key energy projects, subject to there being acceptable business cases:

- A Solar Park at Soham and
- Energy Performance Contracting for public buildings and schools (EnPC Project).

2.2 The Soham Solar Park project has established a positive business case and undertaken pre-application discussions and feasibility with the local planning authority. Early discussions with UK Power Networks identified potential to connect to the local grid in early 2015 and preparations for submitting a planning application are underway.

2.3 The EnPC Project is currently preparing to run a mini-competition to procure an energy supplier and has signed an agreement with the Greater London Authority (GLA) to access a framework contract. Engaging with schools has resulted in forty schools signing up to date for energy performance contracting (providing the business cases for their schools are positive).

2.4 A list of CCC office buildings has been identified which could undergo energy performance contracting to save energy and money over the medium- term and discussions are ongoing as to which buildings to prioritise. Shire Hall and the Octagon have the highest energy consumption and have been identified as pilot buildings.

3. Main Issues - MLEI Project Risks

3.1 Signing a contract for the MLEI Project with the EU in August 2012 was on the understanding that should the MLEI Partnership not deliver the outputs highlighted in section 1.9 above, the EU could clawback some or all of the technical assistance grant, dependent on how much investment is delivered by 21st August 2015. For example, if the project delivers £10million investment it is eligible to retain two thirds of the grant. Consequently, there has, as with all of these types of projects, been some risk for the Council.

3.2 At the time of signing the contract, the risk was considered to be low and acceptable as there were a range of potential projects for delivery and that there was a strong likelihood that we could deliver the required objectives. Since the start of the MLEI project, all but the County Council led projects have fallen away.

3.3 The grant allocation under the MLEI Project for Cambridgeshire County Council is up to £530,000 over three years, with the remainder going to the other partners. By February 2014, £230,000 of the grant has been spent. If the project were to stop now CCC would need to pay back the £230,000 as there is no evidence of any investment committed into projects. If £15million of investment can be evidenced by 21st August 2015 then the full £530,000 can be retained.

3.4 During April and May 2014 delivery challenges on the two key investment projects have increased the clawback risk on the project. The delivery challenges could impact our ability to deliver the investment leverage required by the MLEI contract within the timescales.

The delivery risks on the two projects are described in more detail below.

3.5 The Solar Park Project. Currently there are two delivery risks that need to be managed to bring forward the 10MW Solar Park within the MLEI Project timescales. These are connecting to the grid within reasonable timescales and Government's consultation on financial incentives for large scale solar.

3.6 *Grid connection*. Last year UK Power Networks, the owners and operators of the local electricity network, identified that the Soham Solar Park could connect to the grid in early 2015. However, this connection date has now been delayed due to the local network needing a switching upgrade.

3.7 To manage this problem, a number of meetings have been held with UK Power Networks to identify opportunities to bring forward the connection timescales for the solar park. UKPN identified that the business case to proceed with the switch upgrade at Burwell was approved at their Board during May and that there may be scope to connect to the network by the end of 2015 but this still needs to be confirmed. If connection can be confirmed for the end of 2015, this will allow CCC to make its investment decision on the solar park within the MLEI Project timescales.

3.8 The implications for the MLEI Project is that if the grid connection can not be confirmed for the end of 2015 it is unlikely that CCC could contractually commit its investment for the Solar Park and meet the MLEI timescales. It is important to highlight here that the Solar Park project can still proceed if the connection date is later but this means the investment from CCC would not count towards the MLEI contractual obligations and there is potential for the EU to clawback some grant.

3.9 *Launch of Government's consultation on the financial support for solar PV*. The second challenge is the consultation launched by Government on 13th May 2014 on changes to financial support for solar PV, particularly large scale solar. Currently large scale solar parks are supported by renewable obligation certificates (ROCs). The plan is to change this to a new scheme called 'contracts for difference' (CfD) and for new large scale solar schemes to enter an auction to be awarded a financial contract. The auctions are planned to take place twice a year with a first auction currently planned for 27th October 2014. The consultation is open until July 2014 and further guidance will then be issued on the criteria for the auctions.

3.10 The implications of the Government consultation are mainly based around the auction process. LGSS have reviewed the financial modelling for the Solar Park project and it is envisaged that the business case for the Solar Park will still stack up under the new 'Contracts for Difference' finance arrangements. The main uncertainty is around the criteria for the auctions, how auctions will be managed, how contracts will be awarded and the timescale for this process. It is envisaged that auctions will be run to compete on the lowest cost for producing electricity but there may be other factors too. To deliver this project, it is probably to our advantage financially to try to get into the first

auction. Currently securing a confirmed connection and a planning permission are key criteria for submitting an application to auction.

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3.11 Energy Performance Contracting (EnPC) Project.

The key issues to achieve delivery are

(i) agreement on which CCC office buildings can commit to an EnPC contract at a time of uncertainty around which buildings will remain in our portfolio
(ii) the timescales for decisions by schools to invest and commit to EnPC contracts and
(iii) the challenge for providing financial investments into academy schools.

3.12 *CCC office buildings*: The investment case for energy performance contracting for schools and CCC buildings undertaken in October 2013 was predicated on certain participation levels of CCC office buildings and schools. To achieve £5 million of investment by August 2015, 25% of secondary and special schools, 10% of primary schools and 25% of the CCC office buildings (we planned to keep at that time) need to commit to energy performance contracting by August 2015.

3.13 School sign ups to date have been good and fit within the participation levels identified above. However, there is a challenge agreeing which 25% of CCC office buildings will remain within CCC and be given approval to proceed with EnPC. Currently Shire Hall and the Octagon, the largest energy consumers, have been identified for energy performance contracting provided no other decisions on their use are taken and the next step is to secure commitment for 25% of CCC buildings to participate in EnPC by August 2015.

3.14 *Decision timescales for schools*. An issue that needs careful planning with schools is the decision making process with Governors to approve energy performance contracting. It is estimated that the decision process could be up to 6 months from receipt of investment grade proposals to governor decisions to contract. To manage this timescale challenge, schedules for governor meetings are being identified and timescales for decision making being agreed with the schools to ensure that timely investment commitments can be made.

3.15 *Financial Investments for academies*. One of the challenges for academies is their ability to take out loans for energy measures. Academy schools now have their own legal status and are no longer under the guidance or funding of the local authority, receiving education grant directly from the Department for Education (DofE). An issue is that the Secretary of State currently will not allow Academy Schools to take on loans as this impacts on the government's public borrowing debt levels.

3.16 To overcome this problem and to allow Academies to take out loans for energy efficiency measures, DofE, Department for Energy and Climate Change (DECC) agreed with HM Treasury the setup of a finance mechanism called Salix Finance. Salix Finance can loan funds to Academies at 0% finance, DofE provides the capital and DECC pays the administration costs of the Salix Fund. The mechanism works through DofE withholding education

grant from the Academy School to the value of the loan repayments agreed and then passing this through to Salix. This means that all the transaction remains internal to DofE, money is simply being shifted around and government debt isn't seen to be increasing.

3.17 The issues are

(i) Salix has a limited pot of finance which cannot support the 'scaling up ' of investment into schools at a level and pace that's needed

(ii) the energy efficiency measures it can fund are constrained and payback must be under 8 years and

(iii) private sector or the MLEI L-CIF cannot loan finance to Cambridgeshire academy schools without special dispensations or a new finance model being agreed with DofE, DECC and HM Treasury.

3.18 On the positive side, a local Cambridgeshire school, Impington Village College (IVC), has been working with the DofE on a finance model called a 'managed service' for energy performance contracting. IVC was given permission 18 months ago to implement this finance model for energy performance contracting but due to planning permission delays is only now testing the process. If this 'managed service' model for energy performance contracting continues to work for the DofE, this becomes an exemplar for other Cambridgeshire academies which the MLEI Project could look to adopt and unlock the problem. IVC anticipate approval by 24th June 2014 so it is hoped that progress can be reported verbally to committee.

4. Key issues

4.1 On signing the MLEI contract the risk of clawback was accepted should the investment projects not be delivered by August 2015. As a result of recent structural and financial changes, there is an increased risk that the investments into the energy projects may not be delivered in time for the MLEI contract timescales and some clawback of the grant could happen.

4.2 Based on the risks described in section 3, there are three options for Members to consider:

(i) Stop the project now and pay back the £230,000 grant spent by February 2014 plus any additional costs to date.

(ii) Continue to manage the investment project risks and review the position by December 2014, when more will be known about the solar park grid connection accepting that additional costs will have been incurred

(iii) Continue to manage the investment project risks as best as possible to secure the £15million investment commitments by August 2015

4.3 Although the risk of repayment for the Council has undoubtedly increased, officers' views are that there remains a reasonable chance at this stage that the project can deliver within the required timescales meaning repayment of most or all of the funding would not be triggered. As noted above, if the

decision is taken now to stop the project, all monies so far spent will need to be returned.

4.4 Regarding the MLEI requirements for the set up of a finance and delivery mechanism. It is proposed to continue scoping how the high level Fund strategy presented to Cabinet in January 2014 could bring forward a Cambridgeshire Energy Services Company and what benefits this would bring to Cambridgeshire. This scoping will need to come to Committee by December 2014.

4.5 Officers therefore recommend that the project should continue with a review of the position by December in 2014 on the project risks and the scoping of a Cambridgeshire Energy Services Company proposal.

5. ALIGNMENT WITH CORPORATE PRIORITIES

5.1 Developing the local economy for the benefit of all

The transition from a fossil fuel dependent economy to a low carbon economy requires leadership, innovation and demonstrable commitment to change at all levels, even when things are difficult.

A precondition for a thriving local economy is secure energy supplies. Supporting businesses and our communities to become more energy efficient and self sufficient will provide greater economic resilience to future price volatility. The MLEI Project is providing the organisational framework and one or two of the key building blocks for businesses and communities to help themselves.

5.2 Helping people live healthy and independent lives

Fuel poverty is growing as energy prices rise. With the doubling of energy prices predicted in the next 10 years, evidence suggests that cold homes will bring greater health risks impacting negatively on health budgets and services. Finding local mechanisms to improve energy efficiency and generate local energy could reduce the impact of fuel poverty and costs to the NHS.

There are public health issues associated with fuel poverty. There is a strong relationship between cold temperatures and cardio-vascular and respiratory diseases. Countries which have more energy efficient housing have lower Excess Winter Deaths (EWDs). There is a relationship between EWDs, low thermal efficiency of housing and low indoor temperature.

5.3 Supporting and protecting vulnerable people

See above the issue of fuel poverty and the relationship between cold homes, respiratory and cardio- vascular diseases and excess winter deaths. Fuel Poverty impacts most on the vulnerable in our society.

6. SIGNIFICANT IMPLICATIONS

6.1 Resource Implications

The report above sets out details of significant implications in section 5.

6.2 Statutory, Risk and Legal Implications

Please see sections 3, 4 and 5.
In addition, reputational risk needs to be carefully managed with the EU. As a future source of funding across a wide variety of disciplines it is important that every effort to manage the structural challenges are undertaken to evidence leadership and intent to deliver.

6.3 Equality and Diversity Implications

There are no significant implications..

6.4 Engagement and Consultation Implications

There are no significant implications.

Source Documents	Location
Terms and conditions on the MLEI Contract with EASME	MLEI Project Team
Cabinet Report, Mobilising Local Energy Investment (MLEI), 29th October 2013	CCC Website
Cabinet Report, Mobilising Local Energy Investment 9MLEI), 28th January 2014	CCC Website
Cambridgeshire Renewables Infrastructure Framework 2012	http://www.crif.citizenscape.net/core/
Establishing the community connection for the Green Deal in Cambridgeshire (Report, 2012)	http://www.sustainabilityeast.org.uk/
The Energy Act 2013	https://www.gov.uk/government/collections/energy-act