

**Report of the Chief Officer of the Public Private Partnerships & Procurement Units**

**Report to the Director of Environment & Housing**

**Date:** 30/10/2014

**Subject:** Tropical World energy efficiency scheme

**Capital Scheme Number:** 16669 / TWO / 000

Are specific electoral Wards affected? If relevant, name(s) of Ward(s): Roundhay	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Is the decision eligible for Call-In?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

### Summary of main issues

1. This report provides an explanation of the issues that have contributed to a radical change needing to be made in respect of approvals for an existing scheme called RE:FIT phase 2, which related to energy efficiency retrofits of existing council buildings.
2. In July 2012 the Executive Board approved the injection and consequent expenditure of £1.5million of unsupported prudential borrowing. This was to cover energy efficiency works via a spend-to-save model at 9 sites, which formed a pre-determined 'portfolio' of council assets. Subsequently, E.On were selected as the successful tenderer.
3. Given some unforeseen problems with the first phase of LCC's RE:FIT programme – also managed by E.On – there were some unanticipated delays in moving phase 2 forward. However, one of the sites included in RE:FIT phase 2 was Tropical World in Roundhay and over the past year substantial work had been undertaken towards firming up proposals for a relatively large scheme to be undertaken at that site.
4. The scheme designed will install a biomass boiler at its core and require a site closure agreed for the Christmas period of 2014 to allow for the works to be carried out. Due to the shutdown period and the critical impact of re-opening in time for the February half-term holidays, current timeframes are extremely constrained.
5. Unfortunately, on the 23<sup>rd</sup> of October 2014 E.On announced that they were disbanding the branch of their business set up to undertake energy efficiency works. As a

consequence, E.On have confirmed that they would be unable to take the project at Tropical World any further.

6. Given the urgent need for heating infrastructure upgrades at the site and the beneficial return on investment offered by the available income streams, there is strong support to still proceed with the proposals and an alternative delivery route has been developed to proceed with the plans in order to deliver a broadly equivalent scheme.
7. However, this results in a risk transfer back into the council that would have been externalised under RE:FIT. The remainder of this report sets out the key changes in this respect whilst also elaborating upon the contributing factors.

## **Recommendations**

The Director of Environment and Housing is requested to :-

8. Note that the original approval to inject money into the capital programme granted by Executive Board in July 2012 will remain in place as a 'parent' scheme, with subsequent schemes being brought forward as sub-schemes on an individual business case basis, for which separate approvals will be sought.
9. Authorise spend of £434,254 on the delivery of the energy saving improvements to Tropical World described in this report, to be made up of:
  - £342,040 of prudentially borrowed money;
  - £55,937 from CPM capital maintenance scheme (subject to recommendation 10 below); and
  - £36,277 from a Salix loan.
10. Note that another DCR has been prepared by CPM for consideration by Civic Enterprise Leeds (CEL), which links to this overall scheme and contributes £55,937 to this scheme.
11. Delegate authority for the Chief Officer of Parks & Countryside to sign a loan agreement to allow part of the funding (£41,719) to be provided by the council's Salix Energy Recycling Scheme (SERS).
12. Waive contract procedure rules (CPRs) 8 and 9 (in accordance with CPR27) in order to award contracts without competition to the contractors who will be used to deliver the scheme as listed below and any other contractors which in the opinion of the Chief Officer of Parks and Countryside are required to deliver the scheme:
  - Sayes
  - Synergise
  - RIM
  - Matrix
  - Redding Associates

13. Authorise the immediate issue of purchase orders for the biomass boiler and air handling units (total cost of £106,550) in order to maintain the programme for delivery of the scheme.

## **1. Purpose of this report**

- 1.1 The objective of this report is to explain and rationalise the changes that need to be made to an existing energy efficiency scheme, having been necessitated by a contractor decision that was beyond the council's control.
- 1.2 By virtue of the urgency faced by the council in respect of pursuing an alternative approach in order to still deliver the scheme, there is a requirement for a decision on an urgent, alternative delivery route.
- 1.3 This report provides the detail needed for the appropriate decision-maker to conceptualise the underlying issues that have led to the issues encountered with a view to supporting the justifications underpinning the proposed remedial actions.

## **2 Background information**

- 2.1 RE:FIT phase 2 began in January 2013 and it constituted the 2<sup>nd</sup> wave of the council's corporate energy performance contracting programme.
- 2.2 RE:FIT itself is a framework agreement coordinated by the Greater London Authority. The model provided under RE:FIT contracts is considered to be innovative, owing to the fact that it enables the procuring entity to transfer risk to a 3<sup>rd</sup> party (an energy services company or, ESCo). Essentially, in practical terms this means that the ESCo has to guarantee that a certain level of energy savings will be achieved over the tenure of the contract (the payback period). The logic is that this gives the investing authority surety over its ability to repay whatever loan it has to take out in order to finance the CAPEX costs for installing the required energy conservation measures.
- 2.3 Phase 2 of the council's RE:FIT work has been subject to sizeable delays. A considerable amount of time elapsed between contract award and proposals reaching a point where they could be signed off as viable schemes. Whilst this was disappointing it was a direct result of legacy issues from the 1<sup>st</sup> phase of the programme wherein there was a problem with access to building management systems, which had a detrimental effect on us being able to agree upon a suitable measurement and verification regime. This was closed down as an issue at the start of 2014 and subsequently, there was renewed focus on moving forward phase 2 of our corporate energy performance contracting programme. There have also been performance issues with phase 1 in terms of an energy saving deficit against the contractual guarantee. However, remedial work is underway to address this failing and there are contractual mechanisms in place to protect the council.
- 2.4 Over the past 12 months Tropical World has been the priority in the council's phase 2 programme. The rationale for this focus was primarily the site's pressing need for an upgraded heating system.
- 2.5 The considerable time resource expended by LCC and E.On in analysing the energy saving potential at the site culminated in a proposal that focussed primarily on the incorporation of a biomass boiler. This was to take advantage of a government subsidy designed to increase the adoption of renewables technologies, i.e. the renewable heat incentive (RHI).

- 2.6 Given the nature of the internal works that needed to be carried out at the site with respect to the scheme, the site manager agreed to a building shutdown period of 6 weeks to allow the works to be completed. Considering Tropical World's standing as a very popular Leeds based attraction, the agreement to engage in this closure represents a quantifiable loss of income. The shutdown period was extended specifically to make allowances for this scheme but there are also some other works being undertaken concurrently onsite over the Christmas holiday.
- 2.7 The shutdown created a limitation around timescales, which meant that the programme had to be compartmentalised to a high degree of accuracy in order for the schedule to be met. The main issue in this regard was to ensure that orders for key pieces of equipment were placed before the 'drop-dead' dates for delivery lead-in times.
- 2.8 Biomass generated heat is classed as renewable microgeneration and as such attracts a government subsidy called the renewable heat incentive (RHI). Linked to this, another crucial deadline is the 31<sup>st</sup> of December 2014 as after this point the RHI rates are subject to change. In July 2014 the financial incentives available via the RHI reduced by 5%. In October 2014 the RHI rates were again lowered, this time by 10%. This process is known as degression and its primary purpose is to ensure that the budget set aside by the government for the subsidy can cope with the increasing proliferation of renewable energy projects across the country. Industry observers expect that degression will also occur in subsequent quarters given that the uptake of biomass boilers is increasing way above expectations. The hope is that technological advancements and increased demand will drive down CAPEX costs for the associated equipment to counteract the effect of reducing subsidies but this is not guaranteed, especially over the short to medium term. As such, the importance of achieving the earmarked delivery timescales was reinforced by the recent industry developments that have served to lower the RHI subsidy.
- 2.9 In the week commencing the 20<sup>th</sup> of October the council was on the verge of signing a call-off contract with E.On to deliver the agreed works, having received the necessary planning consents to go ahead with the scheme. However, without any prior warning the contractor announced that they were exiting the energy efficiency market with immediate effect. As such, it was untenable for them to commit to new projects due to a perceived lack of financial reward.
- 2.10 As a result of the above, urgent talks held between key internal stakeholders have yielded a proposed solution that would appear to be the only realistic and pragmatic way in which to deliver a solution in the foreseeable future.

### **3 Main issues**

#### **3.1 Design proposals and full scheme description**

- 3.1.1** The proposal centres on a biomass boiler at its core. This will be fed by European standard compliant wood pellets. The biomass boiler will primarily feed heat into 3 air handling units (AHUs), the 'wet' heat will then be converted into hot air, which will be blown into two of the houses through innovative ducting 'socks' that will distribute it evenly throughout the enclosures. This is highly beneficial to the site since it will provide heat via a much more conducive route than is the case at the

moment, from both a maintenance and perspective. The existing heat is provided by ceiling level 'AmbiRads' in much of the building. These are gas-fired radiant tubes that scorch foliage, are a risk to birdlife, take up undue space, and are costly to service and maintain.

**3.1.2** As part of the additional 'enabling' works associated with the scheme the AmbiRads will be removed in the areas where this is required. In addition, the existing conventional boiler will be replaced with a modern modular boiler. This will solve a problem wherein there is currently only one boiler serving the onsite wet system. The back-up boiler has been condemned due to it being beyond repair. If the existing boiler – which is already ten years old – was to fail, the Butterfly House and other areas of the building would be without heat and flora and fauna could be lost. This scheme will address that issue as part of its wider remit. There will also be heat sharing and exchange between the two separate boiler systems as heating demand fluctuates. Again, this will be beneficial as it will allow the biomass boiler to be used to optimum effect, which will maximise the returns from the RHI. Finally, the building will be controlled and optimised via an industry standard 'intelligent' building management system (Trend IQ). This should ensure that the energy saving plant installed onsite performs to the peak of its abilities at all times.

**3.1.3** When E.On withdrew from RE:FIT phase 2 and Tropical World by association, the project team approached the contract and site managers – Paul Redding and Mark Feugill – formerly employed by E.On with a view to ascertaining their ability to help us to take the scheme forward. They immediately confirmed their interest in providing this assistance and the transition was aided by the fact that both are independent consultants yet have significant knowledge of the project and are immediately available.

E.On were essentially coordinating a cohort of subcontractors and were not to provide any direct organisational labour at Tropical World. This means that by retaining the services of the contract and site managers to the council in place of E.On we are able to deliver an identical scheme to that previously envisaged because they themselves were pivotal in designing and specifying the scheme at Tropical World, as well as in appointing the subcontractors involved. We asked the two individuals – though the contract manager's consultancy firm 'Redding Associates' – to approach the subcontractors that E.On intended to use as they are already geared up to deliver this scheme. This confirmed that the subcontractors involved are prepared to work for the council under similar terms and conditions and maintain the same prices.

The new model will see the council act as principal contractor but with the core responsibilities delegated down to Redding Associates, who will manage the subcontractors onsite.

**3.1.4** The only difference between this proposal and the previous one that was to be delivered by E.On is the loss of the savings guarantee that would have been embedded into the RE:FIT contract. Indeed, it must be noted that if we choose to go down the route supported in this report, there will no longer be a 3<sup>rd</sup> party risk transfer since there will be no contractually embedded savings guarantee. This was a RE:FIT specific facet, which is now lost. This means that the risk for achieving the savings would be borne by the council. However, the returns associated with this scheme flow principally from the government subsidy for biomass heat generation,

i.e. the RHI, and not via gas savings in isolation. Through well-established benchmarks for boiler usage, we can be fairly certain that the 5,000 operational hours earmarked for annual biomass boiler usage will be at least matched and probably exceeded, especially through adoption of a rigorous and consistent building management system (BMS) strategy, implemented by Parks and Countryside staff onsite and monitored remotely by the council's centralised BMS server.

As such, the financial 'savings' (or income) should be relatively secure and hence, the lack of a contractual savings guarantee becomes less crucial than it would be in similar energy efficiency schemes. It is also pertinent to note that the council's other main experience with renewables, a corporate photovoltaic (PV) scheme, has been successful despite the absence of contractually binding levels of performance. In addition, Tropical World is the best possible candidate, internally, for a biomass scheme because it has a year round 24 hour demand for heat.

**3.1.5** As this project will no longer be covered by the RE:FIT contract and the time constraints do not allow the time necessary to put the requirement out to tender, a waiver will be required to award the contract to the applicable contractors without competition. As the values involved in the construction contracts are well below the OJEU threshold for works and the consultancy element also falls under the services threshold, there is no impediment from a contracts procedure rule perspective providing a waiver of some of the contract procedure rules is granted allowing direct award of the necessary contracts without competition.

**3.1.6** Redding Associates have contacted the subcontractors in question and they have agreed to honour their original prices. The organisations are mainly based within the region and their set responsibilities are listed below:

- Sayes (using DES Electrical as a secondary subcontractor) – conventional boiler install, pipework to and from biomass boiler including heat exchanger plates (etc.), pipework from biomass boiler to AHUs, AHU install, hot blown air sock system, electrical wiring, and AmbiRad decommissioning and removal.
- Synergise – biomass boiler installation and commissioning.
- RIM – internal scaffolding.
- Matrix – building management system.

**3.1.7** It is anticipated that 5 separate contracts will be required under waivers; one for each of the above works areas and a final consultancy based contract for the services to be rendered by Redding Associates. The overall values of these 4 workstreams are:

- Heating infrastructure (Sayes) – £215,979
- Biomass boiler (Synergise) – £80,568
- Scaffolding (RIM) – £28,500
- Building management system (Matrix) – £40,277

- Project/contract/site management and design of the overall scheme (Redding Associates) - £27,675
- **Total** = £392,999

**3.1.8** It should be noted that if the RE:FIT scheme didn't go ahead, corporate property management would still have to deal with the burden of the boiler and AmbiRad situation internally. This scheme presents an opportune moment to mitigate this risk before it becomes a serious issue. Given that E.On have lobbied for their subcontractors to maintain the original quotations they made to them for this scheme – and E.On have considerable purchasing power and tight margins that it's unlikely we could match as a council – it would seem sensible to seize the opportunity available.

**3.1.9** If we had to re-procure a scheme that included a biomass boiler installation at Tropical World the site would need to engage in another shutdown next Christmas (in 2015). This would incur further loss of revenue – in the form of lost gate receipts – for the council attraction, which draws in a large number of visitors annually. Indeed, there is an admission from the site that they would struggle to justify another year of disruption. Furthermore, we could reasonably expect that within a 12 month period RHI depression could reduce the incentives available by some 20% and that would be a conservative assumption. At these levels there would be a risk that the financial business case would be such that the project would no longer stack up from a payback perspective.

**3.1.10** To give context to the above, a 20% reduction in RHI – from current levels – would reduce the RHI linked income of this scheme from £34,543 to £27,635 in year one, which equates to a reduction of £6,908. In basic terms, over the 20 year RHI period this amounts to a total loss of revenue just under £140K. The RE:FIT scheme will substantially reduce gas costs but that is countered somewhat by the need to buy biomass pellets. As a result, approximately 92% of the total cost savings are attributable to the RHI payments that the project will liberate. Therefore, the importance of the biomass boiler and the linked RHI payments at current levels in making this scheme work is exemplified.

## **3.2 Programme**

**3.2.1** The projected project plan is viewable at appendix I of this report. The most pressing issue concerns equipment orders as the length of lead-in times could have been prohibitive to the programme if we couldn't place those orders by certain 'points of no return'.

**3.2.2** As such, orders will need to be placed for the biomass boiler (value of £40K) and the air handling units (value of £66,550) immediately. These orders must be placed by Monday the 3<sup>rd</sup> of November 2014 at the latest and will therefore be issued before the rest of the contract documentation is in place. It should be noted that as these pieces of equipment are custom built and will therefore be bespoke to the site, should the orders be cancelled the council will be liable for the full amount.

**3.2.3** The obvious challenge in achieving the tight deadlines reinforces the need for accelerated decision-making.



## **4 Corporate considerations**

### **4.1 Consultation & engagement**

**4.1.1** There has been significant consultation and engagement throughout the history of this scheme. In the early stages of the RE:FIT phase 2 initiative, councillors, section heads, and building managers were briefed extensively. In addition, sign offs were sought from and provided by central finance.

**4.1.2** As the scheme progressed, engagement continued, albeit this was focussed specifically around bringing Tropical World forward ahead of the other buildings that had formed part of the phase 2 portfolio under RE:FIT. The PPPU worked very closely with P&C during this time, in conjunction with CPM, to bring about the best possible outcomes for the site.

**4.1.3** In recent times, engagement has been reinvigorated and senior council officers and the appropriate elected members have been consulted with in relation to developments around Tropical World. Specifically, the following individuals have been briefed:

- Elected members– Cllr Mark Dobson, Executive Board Member Cleaner Stronger safer communities, Cllr Barry Anderson (Scrutiny Chair Safer and Stronger Communities, Roundhay Ward Members.

### **4.2 Equality & diversity / cohesion & integration**

**4.2.1** A screening document was completed in respect of the RE:FIT phase 2 scheme and that process established that a full equality impact assessment was not required.

**4.2.2** In support of the above statement, it is felt that the proposal doesn't affect how our services and/or procurement activities are organised, provided, or located. We're not seeking to change the way in which a service is delivered to the public since this is a standalone project, which doesn't affect anyone directly. Furthermore, the changes made to the building will have no discernable effect on service users, providing only benefits to the council itself and taxpayers in general.

### **4.2.3 Council policies and city priorities**

**4.2.4** Current national and European legislation calls for continued downward pressure on carbon emissions, energy, and water consumption. In December of 2009, the council's Executive Board agreed a 'climate change action plan' for Leeds, which called for a 40% reduction in carbon emissions from the council's operations by April 2021 (compared to a baseline established in 2008-2009). The full council passed a further resolution in January 2010 to extend this aspiration to carbon emissions stemming from the whole city. As part of its 'carbon and water management plan', which covers the period 2011-21, the council wishes to achieve significant annual energy savings and to reduce its carbon emissions.

**4.2.5** Leeds' climate change and NI185 action plans both specifically reference the RE:FIT initiative and in undertaking this second procurement process, we seek to

extend the council's exemplary work in this area whilst continuing to support national and international policy aims at the local level.

**4.2.6** The 'carbon reduction commitment' (CRC) scheme has also been changed following the 'comprehensive spending review' in autumn 2010. The revenue from allowance sales will be used to support public finances, rather than being recycled to participants as was originally intended. This effectively converts the scheme into a tax which means that the liability of the council has increased. Aside from direct energy cost savings, it's estimated that this scheme will save around 328 tonnes of carbon per annum, which equates to a financial saving to the council of approximately £5,000 a year in terms of our obligations under CRC. This saving is not encapsulated within the appropriate financial model but offers an additional indirect benefit to the council outside of this scheme's primary remit.

### 4.3 Resources and value for money

#### 4.3.1 Full scheme estimate

4.3.1.1 The line item detail for CAPEX costs is summarised in the table below:

#### Capital breakdown

		Cost	
BEMS upgrade	1. BEMS upgrade + sensors	£32,400	
	2. Electrical works	£3,877	
<b>Total Salix funded items for BEMS upgrade</b>		<b>£36,277</b>	
Heating improvement	3. 199kW Biomass package + civils	£80,568	
	4. AHU installation	£54,238	
	5. Ductwork installation	£19,776	
	6. Builders work for AHU	£7,309	
	7. LPHW pipework AHU	£39,600	
	8. LPHW pipework biomass	£32,619	
	9. Access for htg install/strip out	£9,000	
	10. Boiler infrastructure upgrades (links to item 13)	£30,000	
	<b>Total on energy saving side (&amp; share of enabling work)</b>		<b>£273,110</b>
	Additional works - classed as enabling - falling outside of 'spend-to-save' element - from 'CPM capital maintenance scheme'.	11. Access for htg install/strip out	£19,500
12. Ambi-rad strip out		£6,814	
13. Heating boiler replacement		£25,623	
14. Connection of extractor fans to enable BMS control		£4,000	
<b>Total enabling works (share of overall covered by CPM)</b>		<b>£55,937</b>	
External project management + site preparation	15. Contract/project manager fees	£25,675	
	16. Site fencing, signage, first aid, etc.	£2,000	
	17. Landscaping onsite to comply with planning conditions.	£2,000	
<b>Total costs for external PM &amp; site preparation</b>		<b>£29,675</b>	
LCC internally capitalised costs	18. Project management	£39,255	
<b>Total LCC specific capitalised costs</b>		<b>£39,255</b>	
<b>Total Salix-funded capital costs</b>		<b>£36,277</b>	
<b>Total prudentially borrowed capital costs</b>		<b>£342,040</b>	
<b>Internal contribution from CPM capital funding</b>		<b>£55,937</b>	
<b>Total CAPEX all items</b>		<b>£434,254</b>	

- 4.3.1.2 A proportion of the funding is to come from Salix, wherein the council holds a centralised recycled fund for these types of scheme. Salix is a central government supported body that provides interest free loans to the public sector for energy efficiency projects. The benefit of using Salix money for some of this requirement is the fact that it reduces the prudential borrowing cost of finance liability, where the current fixed interest rate – chosen internally – is 4.5%. However, Salix approvals need to be expedited as a matter of urgency to secure the necessary funding. Assistance needs to be provided by CPM to facilitate this. Once secured, the funding needs to be transferred into the appropriate capital budget for this scheme, i.e. 16669 / 000 / 000. It should also be noted by Parks and Countryside that the loan agreement they sign will include a 15% uplift on the figure requested.
- 4.3.1.3 A business case has been prepared for the finance performance group (FPG) of the council as mandated by the financial procedure rules (see appendix 2). The FPG group has ratified the business case as both viable and approvable. For reference, the financial model on which that report is based shows that the associated returns are very positive from a financial standpoint. The scheme has a simple return on investment of 241% and a net present value (over 20 years) of £570K. Furthermore, once loan repayments are amortised, the scheme will have an annual surplus from year one.
- 4.3.1.4 In addition to the above, the scheme will reduce the council's CRC obligations by at least £100K over the project's lifetime (£5k multiplied by 20 years) and there will be a significant net maintenance benefit straight away from removing the majority of the AmbiRads within the building.
- 4.3.1.5 A share of the funding is to be provided by CPM. The logic of this is that there are clear synergies between the energy saving component of the scheme and the additional enabling works that the council would need to tackle internally with or without this scheme. As such, it made sense for an internal investment to be made in order to reduce costs later down the line (as well as to address the growing risks that would be posed by the potential failure of aged equipment). The apposite sum is £55,937 and a separate DCR covering this has already been pushed up the hierarchy within CEL. There needs to be agreement that the DCR in question be sanctioned expeditiously and the money cascaded from the applicable CPM budget into the capital scheme relating to RE:FIT phase 2. This is needed to enable payments to be made to the relevant contractors once the scheme is authorised.
- 4.3.1.6 It should be noted that good value should naturally be embedded into this scheme. In support of this assertion, it is salient to reference the fact that the project is based on E.On costings that were achieved on the basis of their considerable leverage in the market. We can reasonably speculate that it is highly unlikely that the council could have obtained similar quotations had it attempted to deliver the scheme by itself. Furthermore, by removing E.On from the equation, we have been able to eliminate their corporate mark-up from the CAPEX items listed in 4.3.1.1. This has had a beneficial impact on the financial model.

## Capital funding and cash flow

Funding Approval :	Capital Section Reference Number :-		16669 / 000 / 000				
Previous total Authority to Spend on this scheme	TOTAL	TO MARCH	FORECAST				
	£000's	2012 £000's	2012/13 £000's	2013/14 £000's	2014/15 £000's	2015/16 £000's	2016 on £000's
LAND (1)	0.0						
CONSTRUCTION (3)	0.0						
FURN & EQPT (5)	0.0						
DESIGN FEES (6)	0.0						
OTHER COSTS (7)	0.0						
<b>TOTALS</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>
Authority to Spend required for this Approval	TOTAL	TO MARCH	FORECAST				
	£000's	2012 £000's	2012/13 £000's	2013/14 £000's	2014/15 £000's	2015/16 £000's	2016 on £000's
LAND (1)	0.000						
CONSTRUCTION (3)	372.766				372.766		
FURN & EQPT (5)	0.000						
DESIGN FEES (6)	0.000						
OTHER COSTS (7)	66.930				66.930		
<b>TOTALS</b>	<b>439.696</b>	<b>0.000</b>	<b>0.000</b>	<b>0.000</b>	<b>439.696</b>	<b>0</b>	<b>0</b>
Total overall Funding (As per latest Capital Programme)	TOTAL	TO MARCH	FORECAST				
	£000's	2,012 £000's	2012/13 £000's	2013/14 £000's	2014/15 £000's	2015/16 £000's	2016 on £000's
CPM capital scheme	55.937				55.937		
Corporate USB	342.040				342.040		
Any Other Income (Salix)	41.719				41.719		
<b>Total Funding</b>	<b>439.696</b>	<b>0.000</b>	<b>0.000</b>	<b>0.000</b>	<b>439.696</b>	<b>0</b>	<b>0</b>
<b>Balance / Shortfall =</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>	<b>0.0</b>

- **Parent scheme number:** 16669 / 000 / 000
- **Title:** Refit phase 2

## Revenue effects

**Prudential borrowing (PB)** – The annual annuity for PB will be £26,294.72, for a period of 20 years, this on the basis of borrowing £342,040 over that time span and applying the council's standard 4.5% interest rate for PB. The cost of finance £183,854 and hence, the total annuity is £525,894. Initially, there will also be an annual charge for the Salix borrowing but this will be repaid within 5 years.

**Biomass pellets** – The cost for this is still to be ascertained as the tender has not yet been released. In the interim, a notional figure of 4.2p/kWh has been used for the purposes of the financial model but it is envisioned that we will achieve a better price than this once we go through a competitive process. E.On were of the belief that based on their market research we should be able to achieve somewhere in the region of 3.6p/kWh. If true, this will only improve the business case. As the pellets will be required for 20 years and the costs will increase broadly in line with RPI, we want to add an annual 3% uplift to the costs set aside for this purpose in the site's budget.

**Measurement & verification (M&V)** – A provisional fee of £750 has been set aside for the appraisal of savings and checking of RHI payments annually.

**Energy costs** – Although there will be additional revenue implications relating to the purchase of biomass pellets, this will be cancelled out by gas and electricity savings made onsite via the scheme. In the first year, it is anticipated that £50,088 will be saved on gas bills and £1,949 on electricity. Moreover, it is expected that the impact of the gas and electricity savings will increase annually due to fossil fuel inflation being forecast to be at least double that of biomass fuel.

**Maintenance** – the maintenance ‘burden’ introduced is essentially as follows:

- Biomass boiler (first 5,000 hours of operation) – £950
- AHU servicing (2 visits including filter changes) – £2,292
- Modular boiler (2 visits, labour only) – £840
- **Total** = £4,082

However, there is also a substantial saving in terms of no longer having to scaffold up to and maintain the AmbiRad system, which will be decommissioned and removed as part of this scheme. The existing maintenance costs for the servicing of the affected AmbiRads and the existing boiler was quantified by CPM as £8,080. As such, in year one there is a net benefit of £3,998 (= **-£4,082**+£8,080). Therefore, CPM will save money from its centralised maintenance budget. The change will be neutral to the site because they don’t pay for this maintenance themselves but it still provides a positive impact to the overall business case.

However, the site/CPM will still need to make arrangements to find expertise – internal or external – that can be used to provide the required maintenance. It should be noted that the allowance made for maintenance will need to increase with ‘RPI’ (at a selected rate of 3%) year on year. Given the urgency of the works it is proposed that arrangements for servicing and maintenance are dealt with once the works are underway.

**RHI** – in terms of the entry for ‘external income generated’, the figure offered is attributable to RHI. The exact mechanism for how this will be paid to the council is still to be clarified; however, this is the figure that we envisage receiving in the 1<sup>st</sup> year. Thereafter, the RHI will be index-linked and as such, will increase over time. This is important because the relevant inflationary rises in different cashflow items all feed into the financial model and indeed, the payback terms.

**Net effects** - The overall net annual revenue implications in the 1<sup>st</sup> year – for the council as a whole\* – are shown in the formula below:

- (£49,165 wood pellets + £26,295 prudential borrowing + £8,344\*\* Salix repayment + £4,080 introduced maintenance costs + £750 M&V) - £52,037 energy savings - £34,543 RHI - £8,080 maintenance savings
- = **-£6,025** (net benefit)

\* *The site does not pay its own maintenance costs; these are covered via centrally administered CPM budgets.*

\*\* *The Salix repayments will only stand for 5 years.*

#### **4.4 Legal implications, access to information, and call-in**

- 4.4.1** No sections of this report are restricted under the access to information rules.
- 4.4.2** This is a Key Decision but, due to the exceptional circumstances outlined in this report it is being taken under the rules for Special Urgency.
- 4.4.3** The Chief Officer Parks and Countryside met with the chair of the Safer and Stronger Communities scrutiny board and both parties have agreed that the decision is urgent and cannot be reasonably deferred. The basic reasons for urgency are: (i) the contractor intended to carry out these works within the remit of previous approvals has withdrawn from the scheme without notice (ii) the scheme has significant financial and operational benefits for the council (iii) these benefits will not be realised if certain operational and financial deadlines are not met. In order to meet these deadlines this decision must be taken now.
- 4.4.4** Details of this decision will be included in the Leader's report to Corporate Governance and Audit Committee
- 4.4.5** A waiver of the council's contract procedure rules 8 and 9 is required to allow the direct appointment of contractors without competition for the reasons outlined in this report.
- 4.4.6** PPPU/PU will work with Parks and Countryside and Corporate Property Management to put appropriate contracts in place with each contractor.

#### **4.5 Risk management**

- 4.5.1** The individual consultants we wish to contract with are more than qualified to provide the services we need to deliver this scheme successfully. They have combined experience in excess of 50 years in pertinent disciplines and have appropriate insurances to cover their work. The work they provide will cover all the constituent elements that we need in areas that the council itself does not have a great deal of experience in delivering. The rates they are proposing to charge are deemed both reasonable and representative of the task at hand. The fact that a market leader, E.On, employed them should give extra comfort. Indeed, as the principal designers of the scheme to be delivered their continued involvement offers the least risky strategy to take the project forward.
- 4.5.2** Corporate property management will provide site management support. This helps to alleviate the risk that the subcontractor management and liaison role outsourced to the applicable consultancy is not mismanaged and indeed, that tasks are not kept to timetable.
- 4.5.3** A provisional sum of £750 per annum has also been set aside within the model to allow the PPPU to help measure and verify the associated savings and RHI payments over the 20 year period. This is a relatively small sum of money but it will at least allow for independent assessment of performance at regular intervals.
- 4.5.4** In terms of the lost savings guarantee, the risk is lessened somewhat by the fact that the building management system that will be installed will help to ensure that the biomass boiler generates the right level of heat in order for RHI income

expectations to be met. In doing so, the integrity of the financial model will be preserved.

- 4.5.5** The non-domestic RHI provides financial support for renewable heat technologies for the lifetime of the installation (for 20 years). Payments are made on a quarterly basis and those disbursements begin to accrue from the date of accreditation for the installation. The date is confirmed in a confirmation letter emailed to successful applicants. Redding Associates are going to prepare the RHI application on our behalf, which is advantageous given that the council has not processed an RHI application before in its own right.

The fact that the government has guaranteed the scheme for 20 years helps to provide assurances around the soundness of the investment.

## **5 Conclusions**

- 5.1 Given the urgency created by E.On's sudden withdrawal from the energy efficiency market, which came on the eve of the council signing contracts for work to go ahead at Tropical World, the alternative option presented offers the only pragmatic solution that's achievable within the timescales faced.
- 5.2 This is further emphasised by the site's need to improve its heating infrastructure, where works need to be delivered during a pre-agreed shutdown period covering the Christmas holidays (in 2014). Indeed, expectations had been raised as per promises made under the RE:FIT phase 2 initiative and the site had persevered with its heating related problems on the basis of the scheme going ahead.
- 5.3 Capital of £1.5m has already been injected for RE:FIT phase 2 and in light of the Tropical World scheme being almost identical to the one that was to proceed under E.On's direction, it is proposed that the injection remains in place as a parent scheme and the Tropical World scheme be approved as a sub-scheme. Any subsequent proposals for works at additional sites will be brought forward as sub-schemes and approvals sought on an individual business case basis.
- 5.4 The risk profile is considered to be acceptable by the council on the basis of the appropriate safeguards that will be maintained. In support of this, the council's FPG has vetted the business case for the scheme and approved it as being worthwhile to pursue.
- 5.5 Key stakeholders have been consulted and there is strong internal appetite to proceed with the project.

## **6 Recommendations**

The Director of Environment and Housing is requested to:-

- 6.1 Note that the original approval to inject money into the capital programme granted by Executive Board in July 2012 will remain in place as a 'parent' scheme, with

subsequent schemes being brought forward as sub-schemes on an individual business case basis, for which separate approvals will be sought.

6.2 Authorise spend £434,254 on the delivery of the energy saving improvements to Tropical World described in this report, to be made up of:

- £342,040 of prudentially borrowed money;
- £55,937 from CPM capital maintenance scheme (subject to recommendation 6.3 below); and
- £36,277 from a Salix loan.

6.3 Note that another DCR has been prepared by CPM for consideration by Civic Enterprise Leeds (CEL), which links to this overall scheme and contributes £55,937 to this scheme.

6.4 Delegate authority for the Chief Officer of Parks & Countryside to sign a loan agreement to allow part of the funding to be provided by the council's Salix Energy Recycling Scheme (SERS).

6.5 Waive contract procedure rules (CPRs) 8 and 9 (in accordance with CPR27) in order to award contracts without competition to the contractors who will be used to deliver the scheme as listed below and any other contractors which in the opinion of the Chief Officer of Parks and Countryside are required to deliver the scheme:

- Sayes
- Synergise
- RIM
- Matrix
- Redding Associates

6.6 Authorise the immediate issue of purchase orders for the biomass boiler and air handling units (total cost of £106,550) in order to maintain the programme for delivery of the scheme.

## **7 Background documents<sup>1</sup>**

7.1 Appendix 1 – programme Gantt chart

7.2 Appendix 3 – FPG business case report

7.3 Appendix 3 – financial model (pdf)

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<sup>1</sup> The background documents listed in this section are available for download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.