

## Cheltenham Borough Council

**Cabinet – 09.02.2016**

### Future Energy Purchasing for Cheltenham Borough Council

<b>Accountable member</b>	<b>Cabinet Member Clean and Green Environment, Cllr Chris Coleman</b>
<b>Accountable officer</b>	<b>David Roberts</b>
<b>Ward(s) affected</b>	<b>ALL</b>
<b>Key/Significant Decision</b>	<b>Yes</b>
<b>Executive summary</b>	The Council at present has a short term agreement with UX Energy Services to act as a broker for CBC to procure energy. The contracts procured by UX Energy with the energy suppliers expire in April 2016 and require replacement. To facilitate this a new energy procurement exercise has been undertaken working in partnership with our 2020 Partners from West Oxfordshire District Council, Cotswold District Council and Forest of Dean District Council and will ensure that the Council has gas and electricity supplies for the next 4 years along with our 2020 partners. Since the expenditure on the contract is over £100k, it is a key decision, requiring cabinet approval.
<b>Recommendations</b>	West Mercia Energy (WME) should be appointed as CBC energy supplier under their framework.

<b>Financial implications</b>	The costs of using the WME framework will be embedded within the energy prices secured on behalf of CBC, and no direct cost will arise as a result.  <b>Contact officer:</b> <a href="mailto:Nina.Philippidis@cheltenham.gov.uk">Nina.Philippidis@cheltenham.gov.uk</a> , 01242 264121
<b>Legal implications</b>	The WME framework is EU compliant and the framework has a standard contract that the council will be required to enter into.  <b>Contact officer:</b> <a href="mailto:Sarah.Halliwel@teWKesbury.gov.uk">Sarah.Halliwel@teWKesbury.gov.uk</a> , 01684 272692
<b>HR implications (including learning and organisational development)</b>	No direct HR implications arising from the contents of this report.  <b>Contact officer:</b> Julie McCarthy <a href="mailto:Julie.Mccarthy@cheltenham.gov.uk">Julie.Mccarthy@cheltenham.gov.uk</a> , 01242 264355
<b>Key risks</b>	<b>Not agreeing supplier and having to pay emergency rates until a new supplier can be appointed.</b>
<b>Corporate and community plan Implications</b>	None of a significant nature identified and this procurement should be neutral in effect.

<p><b>Environmental and climate change implications</b></p>	<p>At this stage, it has been important to determine that green electricity can be purchased through the chosen model. WME has confirmed that green electricity can be purchased, but has noted that a premium is payable because of the removal of the exemption from the Climate Change Levy (CCL) for renewable sources of electricity.</p> <p>At the point where electricity is being procured, therefore, the council will need to understand the impact of the removal of CCL and the resulting differential between green and brown electricity, in order to make a decision about whether to continue procuring green electricity.</p> <p><b>Contact officer:</b> <a href="mailto:Gill.Morris@cheltenham.gov.uk">Gill.Morris@cheltenham.gov.uk</a> 01242 264229</p>
<p><b>Property/Asset Implications</b></p>	<p>Comments from Property and Asset Management are included in the body of the report</p> <p><b>Contact officer:</b> <a href="mailto:David.Roberts@cheltenham.gov.uk">David.Roberts@cheltenham.gov.uk</a> 01242 264151</p>

## 1. Background

Since gas and electricity markets opened to competition in the 1990's, the energy market has become a highly specialised field of procurement. The complexity of the procurement options can create a risk if not managed by someone with the appropriate level of skills and expertise. It is also time consuming due to the potential number of suppliers and types of contract available.

In recent years the energy contract options have developed considerably with a range of procurement options available and with increasing complexity requiring specialists to manage. For example, Flexible purchasing relies on specialist buyers monitoring the market on a daily basis to ascertain the best opportunities to purchase energy, including advance purchasing. Specialist support is required to ensure value for money and appropriate risk management levels are applied.

Several buying organisations, both private and public sector, can secure such contracts on the Council's behalf. Public sector buying organisations (PBOs) are favoured because they focus solely on public sector needs rather than trying to match the potentially competing objectives and requirements of private and public sector organisations. In addition, these groups have long experience of acting on behalf of the public sector and are therefore well versed in their requirements and processes. The frameworks that offer this service have been procured in accordance with EU Directives and comply with the Public Contract Regulation.

The Council has used UX Energy Services a non PBO for the last year after negotiating a year extension to their existing council framework and CBC now needs to be able demonstrate best value and compliance with the Public Contract Regulations for its future needs.

The task of looking at procurement of energy was considered by a group consisting of representatives from the 2020 Partners, Go Shared Services Procurement Team, Oxford County Councils Procurement Team, (on behalf of West Oxford Council) and the City of Oxford Energy Team, (through Links with Oxford County Procurement Team) who were tasked with procuring energy for all the partner councils.

## 2. Alternative options considered

- 2.1 Option 1 do nothing – not a real option as the Council needs a supply of energy to function and deliver its services. If not managed properly and energy contracts are not secured, out of contract “deemed” rates would be incurred meaning significant increases in energy costs at a time when budgets are getting increasingly constrained.
- 2.2 Option 2 run a procurement process in-house to either purchase energy itself or go to the market for a broker to buy on its behalf– this would be a costly exercise that would not necessarily guarantee value for money for the Council. CBC does not possess the specialist trading knowledge that is essential for operating within the energy market. The Council would also not be able to procure energy flexibly itself direct from the wholesale market due to its volumes being too low. The volumes that the Council will need to purchase would also not be as attractive as a stand-alone client for energy suppliers compared to aggregating purchase through a third party such as a PBO and using the collective purchasing power to secure the most competitive rates. The procurement would be above the EU threshold and therefore would be subject to EU procurement rules. In a volatile market such as energy supplies, the supplier will load the costs as during the standstill period energy prices can fluctuate and this would not give the best value for the councils.
- 2.3 Option 3 use a public (professional) buying organisation (PBO) or third party intermediary (TPI) buying organisation PBOs/ TPI's act on behalf of a client to purchase its energy and related services for a commission. This is a fast and growing area with both not-for-profit public sector focussed (PBOs) and profit driven private sector players on the market. Whilst there are a

number of reputable and well-established private sectors organisations available, not all of these organisations procure energy in accordance with the Public Contract Regulations. PBOs which buy solely for the public sector ensure that they comply with EU procurement directives and the Public Contract Regulations. PBO's, therefore, present a closer match to local authority purchasing requirements, whilst the market is developing (and as the TPI codes of practice is still being developed by Ofgem )it is safer to work with a PBO for the next energy purchasing framework period The developing market and procurement options will continue to be tracked and monitored with a view to future decisions on our approach to Energy (and in future water) purchasing. PBOs offer a fully managed, flexible and risk managed approach to energy purchasing and commonly has dedicated teams, experienced in energy trading that provide a compliant route to market for public sector organisations. There are various PBOs available to local authorities to procure energy, with some of the main PBOs as follows:

- Crown Commercial Services (CCS)
- Eastern Shires Purchasing Organisation (ESPO)
- London and South East Region (LASER)
- West Mercia Energy (WME)
- Yorkshire Procurement Organisation (YPO).

**2.4** The option of using a PBO for the reasons given above was felt to be the most appropriate approach following discussions with Go Shared Services, Oxford County Procurement, working for West Oxford, a representative from West Oxford a representative from CBC and the Oxford City Energy Team. The group looked at performance of the PBOs and the services offered. However it was difficult to back-test performance of the various PBOs to gauge what energy costs may have been, given the fact that energy purchasing is happening in a dynamic way on a daily basis and this sets the final price secured for a set purchasing period which were not comparable. From the evidence the offerings available from the various PBOs were generally similar with some offering more flexibility and a wider range of extra options. CCS for example do not offer as wide a range of support, which was felt was required by CBC and ESPO are a joint offering with Laser, so they were dismissed as the Lasers offering was earmarked for more in-depth consideration. From this process, given the time constraints, and the similar levels of service on offer from the various PBOs, it was decided to focus on two major PBOs, based on existing 2020 Partners experience of use of their services. LASER, employed successfully by Oxford City Council for the last 3 framework periods (also used by Oxfordshire County Council and other authorities in Oxfordshire – such as Cherwell District Council and West Oxon District Council) and WME – employed by Cotswold District Council , Forest of Dean Council, Tewkesbury Borough Council and Gloucester City and County Councils:

**2.5** Option 4 an additional option was explored for CBC looking at its existing supplier UX Energy, a TPI, this option is not recommend it for the following reasons

- The existing framework they offered was not felt to comply with the OJEU regulation, and is due to expire in 2016
- The closer match of a PBO as opposed to a TPI for supplying CBCs needs
- The proposed replacement framework was not in place and has not been through the OJEU process as yet and therefore there is a risk of it not reaching a successful conclusion in time for our needs and questions still remain about the suitability for CBC use.

- Finally the cost model showed the management fees would be higher than the WME model, though this is a hidden fee and might not reflect in the final costs paid by CBC for its energy

**2.6** As part of the procurement exercise a set of questions of areas of requirements for service delivery were used and the 2 leading PBOs Laser and WME gave presentations to the 2020 group looking at the procurement process. Following the presentations and further group discussions the WME model and services was felt to most closely match CBCs needs.

**2.7** A Cost comparison of the management fees levied by the suppliers was undertaken looking at Laser, UX Energy and WME, however, it proved difficult to compare directly as each model achieves the required income in different ways but from the figures provided and modelled for CBC on our present use the WME model appeared to provide the best VFM

### **3. Reasons for recommendations**

**3.1** Following the process described in section 2 and conversations with framework suppliers representatives from Oxford City Council, West Oxfordshire District Council, Cotswold District Council and Cheltenham Borough Council considered which framework would be the best suited for each authority, the view collectively was that the WME offer was a better match for the 2020 Partner Councils including CBC for the following the reasons

- WMEs performance has been better than the industry average
- WME operate a trading gains sharing scheme with the user Councils
- The WME operating cost recovery model for their fees is the lowest of the 3 looked at, (however this cost is not always visible as it is collected from the electricity producers)
- WME have a successful track record of delivering to some of the 2020 Partner councils
- The match of the energy purchasing model was identified by Oxford Cities Energy Team as the best match to CBCs portfolio
- The Partners have experience of WME and have already developed a working relationship
- The WME Offices are relatively close to CBC and their business is concentrated in supplying Councils in the South West and West Midlands, giving easier access to support
- The partner councils are recommending that WME is their provider and this procurement will therefore bring CBC in line with the other 2020 Partner Councils
- WME is also developing further energy management services as part of their packaged service
- WME offer a fully managed procurement service only meaning that energy bills are validated and processed by WME prior to passing on to the customer for payment. This level of support is important for the Councils due to limited in-house skills and resources, but this is at an additional cost which CBC will need to make allowance for. ( This cost was included in the cost model and WME were still notionally the best VFM)
- Overall the support services offered by WME were the felt to match CBC needs best ( Again there will be fees for any services)

- This framework offers fully flexible purchasing, with the ability to trade ahead of and within financial year
- WME offers a capped price in line with the financial year, which gives 12 months budget certainty. In March of each year WME communicate the capped energy price for the forthcoming financial year, which is the maximum that a customer will pay
- If wholesale prices increase there is no reconciliation resulting in further charges to be paid. The capped price is then reviewed in August and December to determine if any discounts off the cap can be given
- Access to the WME website which has consumption data and reports
- Bills come from WME not the supplier making billing easier.

#### **4. Consultation and feedback**

- 4.1** This procurement process has been developed with the Director of Resources, The project team, the GO Shared Services Procurement Team , Oxford City Council Energy Team, and consultation with Finance Legal and HR.

#### **5. Performance management –monitoring and review**

- 5.1** WMEs offer includes various management and performance review opportunities including the following which will enable CBC to input and feedback on the performance of WME

- a. Quarterly reviews discussing portfolio and billing issues
- b. Annual pricing meeting (Late Feb/early March)
- c. Termly pricing decisions (usually price set in March maintained for year)
- d. Position statements reviews :
  - October (half year position)
  - December (ahead of pricing for final quarter)
  - February (linked to pricing meeting)
  - July (final one)
- e. Energy Manager group meetings :
  - South West group
  - All customers.

- 5.2** The in house CBC capacity for the management of the energy contract and ongoing opportunities and risk associated with energy use needs developing as the resource and capability in the Council is limited and this will need to be developed to maximise the benefits of the contract.

- 5.3** In addition WME have their own internal controls and risk management including the following
- Energy Governance Accountability Risk and Reporting Policy

- Daily Internal purchase meetings
- Daily value at risk reporting
- Daily phone calls with external third party market analysts
- Bespoke system developed to manage queries
- Full audit trail of phone calls, letters, emails attached to customer accounts.
- Regular supplier meeting to manage/escalate queries
- Letters/accruals issued to customers

This can be monitored by CBC working in partnership with WME.

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<b>Appendices</b>	1. Risk Assessment

Risk Assessment

Appendix 1

The risk				Original risk score (impact x likelihood)			Managing risk				
Risk ref.	Risk description	Risk Owner	Date raised	Impact 1-5	Likelihood 1-6	Score	Control	Action	Deadline	Responsible officer	Transferred to risk register
	If there are cost variations between "green" and "brown" energy tariffs then the council will need make a judgement about which supplier to use this may not favour the green supplier then reduce the rate of discount to the prevailing Climate Change Levy (CCL)	Head of Property Services	01.10.2015	2	6	12	Report to be developed when the framework set up to compare and report to Cabinet on implications	The greenest sources of energy will be sourced where viable for the quarterly supplies on fixed term contract - but this will need to be reviewed in the light of the reduction to the rate of discount to the prevailing rate of (CCL)	Ongoing	Building Surveyor	NA
	If we use brown energy then our carbon emissions will increase with the knock on effects to	Head Of Property	01.12.2015	2	3	6	Reduce energy use continue with green energy	Investigations of likely outcomes of using brown energy and review our energy strategy and	April 2016	Building Surveyor	

	global warming both for biodiversity and more extreme weather effecting the cost of running our property stock							plans of action to reduce carbon emissions			
	If there was a global incident e.g. war, natural disaster etc. that materially affected the supply/ price of gas / water / electricity then this may have a significant impact on the cost and supply of energy	Head of Property Services	02.11.2015	3	4	12	Transferred to Supplier	Complete analysis tools such as Kraljic, supplier referencing, Porters 5 Forces, etc. this will result in regular monitoring reports being provided by the supplier to CBC this will enable a joint response to be developed to any threats or price increases	monitored by property services	Teambuilding Surveyor with Procurement support	
	If the price of energy drops significantly during the	GO Shared Services Procurement team	01.04.2015	2	2	4	Accept	The contract would be locked in for a four year			

	period of the contract then the council would be unable to change supplier							framework period with billing coming from WME, there is some flexibility to discuss with WME the price variation in the contract			
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**Explanatory notes**

**Impact** – an assessment of the impact if the risk occurs on a scale of 1-5 (1 being least impact and 5 being major or critical)

**Likelihood** – how likely is it that the risk will occur on a scale of 1-6  
(1 being almost impossible, 2 is very low, 3 is low, 4 significant, 5 high and 6 a very high probability)

**Control** - Either: Reduce / Accept / Transfer to 3rd party / Close