MUNICIPAL YEAR 2018/2019 REPORT NO. 187

MEETING TITLE AND DATE:
Cabinet - 12th March 2019

REPORT OF:
Director - Commercial

Contact officer and telephone no:

Nicky Fielder tel: 0208 379 2016

Email: nicky.fiedler@enfield.gov.uk

Agenda – Part: 1	**Item: 6**

Subject: Update on the Council's Approach to Funding the Remainder of Energetik's Business Plan (i.e. tranche 2)

Wards: All Wards
Key Decision No: KD 4859

Cabinet Member consulted:

Cllr Ahmet Oykener

1. EXECUTIVE SUMMARY

1.1 In October 2018, Cabinet approved Energetik's proposal to further explore different funding options, including approval to explore a formal proposal from the Mayor's Energy Efficiency Fund (MEEF) and to establish the details of such alternative funding (see Cabinet Report entitled 'Energetik Funding Options').

1.2 This report sets out the different funding options that have been explored and the reasons the alternative options have been discounted. It seeks agreement on the shareholder strategy and approval of the preferred funding route for the Company to take forward. A second paper will be submitted by autumn 2019 to secure the second tranche of investment for Energetik's business plan.

1.3 Following approval to pursue the preferred option, the necessary steps will be taken to establish more detailed terms and conditions. During this time, Energetik will be updating its business plan and will work with the council to undertake the required due diligence. A further report will then be submitted to Cabinet by autumn 2019 to agree the final investment decision.

1.4 Depending on the option selected, the Council has the opportunity to ring-fence some of the interest premium returns it will receive from the company for use in fuel poverty projects, enabling the benefits derived from Energetik to be shared with a greater number of Enfield residents. This is as a result of an improvement in the funding environment in this sector.

2. RECOMMENDATIONS

2.1 Notes the contents of this report.

2.2 See Part 2 Report

2.3 Notes that a further report will be submitted to Cabinet by autumn 2019 to agree the actual investment decision once the outcomes of the preferred funding option have been approved and the due diligence on the updated Company Business Plan is complete.

2.4 See Part 2 Report

3. BACKGROUND

Overview and context

3.1 In January 2017, the Council's main investment decision in the Energetik Business Plan was approved by Cabinet, with a phased approach to investment to help manage the Council's risk exposure. The investment decision essentially set out a two-phase approach and comprised:

a) An initial tranche 1 for previously identified expenditure to the capital programme was included and sufficient new loans to meet energetik's financial needs until 2019 (£10.63m).

b) A forecast expenditure allocation to the indicative capital programme for tranche 2, the forecast remaining investment required to deliver the full Energetik Business Case from 2019 (£39.5m); an additional forecast expenditure allocation to the indicative capital programme for a Business Expansion Fund (£4m) was also required. This second tranche was to be applied for following the completion of Energetik's heat sale agreement with the North London Waste Authority (NLWA) and upon the council entering into its Master Developer Framework Agreement (MDFA) with its preferred bidder at Meridian Water, as this would determine the final borrowing requirements and future cashflows of Energetik.

3.2 In October 2018, Cabinet asked Energetik to seek alternative funding sources to be fully appraised of the options available to the Council as shareholder. This included approval to explore the Mayor's Energy Efficiency Fund (MEEF) and to establish the details of such alternative funding arrangements that may be available (see Cabinet Report entitled 'Energetik Funding Options').

3.3 This report provides an update on the progress made with the various funding option, and seeks to establish a co-ordinated view of the current shareholder position in terms of investment options, so that the favoured option can be developed further ahead of a final decision on the Company's Tranche 2 investment decision.

3.4 The Company requires a final investment decision by autumn 2019 to ensure it can deliver its business plan and meet its obligations.

3.5 A further report will be submitted to Cabinet by autumn 2019 to agree the actual investment decision once the above outcomes of the preferred funding option have been approved and the due diligence on the updated Company business plan is complete.

3.6 – 3.25 See Part 2 Report

4. ALTERNATIVE OPTIONS CONSIDERED

4.1 Overall, doing nothing is not possible as energetik has current commitments to its existing customers and clients at its active and in development heat networks.

4.2 A delayed decision to invest will mean significant cost increases to the Company to deliver its infrastructure due to the expiry of a fixed price agreement with its design and build contractor. In turn this reduces the potential retained earnings in the business and increases the amount of loans required.

4.3 – 4.8 See Part 2 Report

5. REASONS FOR RECOMMENDATIONS

5.1 – 5.5 See Part 2 Report

6. COMMENTS OF OTHER DEPARTMENTS

6.1 Financial Implications

6.1.1 In line with the Council's Treasury management strategy a Council owned company will need to meet the following requirements before the Council agreed to on lend:

a. An independently reviewed business case and cash flow forecast - signed off by the Director of Finance.
b. Demonstrate the ability to repay both interest and principal over the agreed repayment schedule.

c. Where possible the Council will secure the loan on the Company assets.

6.1.2 This acts as a basis to ensure that the risk of loss to the Council is minimised. If these requirements are seen to be adequately met, the Treasury Team will then proceed to consider the best mix of loans to ensure the most advantageous blend are achieved.

6.1.3 In assessing the suitability of a loan provider, the following assessment will the considered:

a. The governance arrangements and conditions/penalties around the loan.
b. The duration of loan and timing of loan drawdown.
c. The interest rate.
d. Flexible around principal repayments.
e. State Aid issues.

6.1.4 It is proposed that funds will not be on lent to Energetik until they can adequately demonstrate that contracts are in place and expenditure is ready to be committed. A facility will be put in place but there will be a formal drawdown process.

6.1.5 Given the interdependency on the build-out of the Meridian Water project and the risks around delivery of the project, it is recognised that loan commitments to Energetik should be limited so that the Company does not become over-extended with loan debt.

6.1.6 The Council will need to recognise in its statement of accounts the degree of risk of failure attached to the loan, given the uncertainty around future income streams coming from Energetik and the limited amount of realisable assets that the Company own.

6.1.7 Energetik will be required to provide the Director of Finance a quarterly report on the progress of the project via the on-lending agreement.

6.1.8 Due to State Aid rules the on-leading to the Company will result in the Council having to charge Energetik an interest premium of between 2.5% - 4% on the actual cost of borrowing. This will depend on the nature of the expenditure incurred. The interest ‘premium’ will be set off against the Council’s total interest paid budget. It is anticipated that the interest rate premium will be greater than Tranche 1 from 3rd party lenders.

6.1.9 Should any interest premium be ring-fenced for investment in fuel poverty activities the financial impact of this will need to be considered as part of the medium term financial plan and included in future net interest budget forecasts.

6.2 Legal Implications

6.2.1 The Council has the power under s.1(1) Localism Act 2011 to do anything which individuals generally may do provided it is not prohibited by legislation and subject to public law principles. Further statutory powers exist to establish and invest in energetik, and S.1 of the Local Government Act 2003 permits the Council to borrow and lend (subject to complying with the Prudential Code for Finance in Local Authorities).

6.2.2 The introduction of the ‘general power of competence’ under the Localism Act 2011 enables local authorities to explore innovative solutions to deliver more with less, generate income by charging and trading and to provide indemnities and guarantees. The legislation provides that ‘a local authority has power to do anything that individuals generally may do’. This includes giving guarantees. However, other restraints of public law still apply. The most relevant of these is that local authorities have a fiduciary duty to act prudently with public monies entrusted to them and must establish (and maintain a full audit trail to support) that the underlying transaction being guaranteed by the Council is itself ‘intra vires’ and that it has been given due and proper consideration in accordance with the normal public law considerations.

6.2.3 When deciding whether to provide assistance such as a loan or Parent Company Guarantee (PCG), the Council should carefully consider the associated risks also ensuring it considers ‘Best Value Principles’ under the Local Government (Best Value Principles) Act 1999. The terms of any loan, PCG or other form of assistance should be subject to legal and commercial due diligence and the final terms of any associated agreement should be in a form approved by Legal Services. In making its decision the Council must also be mindful of the impact of such a decision on any existing loan / funding agreements and PCGs already in place.

6.2.4 It is crucial that before any decision is made, the Council obtains full state aid advice in relation to the project as a whole from both legal and financial experts.

6.2.5 The Council must ensure that it adheres to its Constitution at all times, when making decisions. In addition, as the content of this

Report constitutes a key decision, the Council must ensure the Key Decision process is followed.

6.3 Property Implications

6.3.1 Due to the subject nature of this report, Property Implications are not applicable.

7. KEY RISKS

7.1 Failure to find and approve an agreed funding route in time and therefore not reaching an investment decision by autumn 2019 will have an impact on the company's programme of works, which could have an impact on its ability to meet its obligations.

7.1.2 Mitigation – funding options have been investigated and scoped and this report seeks approval of the preferred funding route for the Company so that a final investment decision can be made by autumn 2019.

7.2 Encountering delays or rejection with successful funding applications and meeting their respective timescales.

7.2.1 Mitigation – to use PWLB as a fall-back mechanism to bridge any delays with funding application timetables.

7.3 Further delays to appointing a developer for Meridian Water and the consequent delay to building homes may have an impact on the quantum and timing required loans by Energetik due to there being a commensurate delay to Energetik's revenues and profit.

7.3.1 Mitigation – ensure flexibility in loan terms e.g. payment holidays, flexible and timely drawdowns etc.

7.4 Failure to reach agreement on the way forward by autumn 2019.

7.4.1 Mitigation **–** as above, EMT and Members are engaged to agree the approach.

7.5 Making isolated decisions on Meridian Water and Energetik and failing to see the overall net impact on the Council.

7.5.1 Mitigation – continued programme review via the interdependency board to ensure all decisions relating to Energetik and Meridian Water consider the impact on each other prior to any decision being made.

7.6 See Part 2 Report

8. IMPACT ON COUNCIL PRIORITIES

8.1 Good homes in well-connected neighbourhoods

8.1.1 Energetik is helping contribute to the Council's regeneration aspirations, providing a low-carbon and sustainable heating solution.

8.1.2 Energetik's Business Plan is aligned with Council priorities. The Company was set up to improve the service offered to its residents living on heat networks developed in the borough by offering better quality standards at an affordable price, whilst being better for the environment.

8.2 Sustain strong and healthy communities

8.2.1 Community engagement and enabling is a cornerstone of the business' delivery model. This in turn promotes stronger, more cohesive communities and active citizenship. The community impact of the project can be described as follows:

- An innovative approach to community engagement will ensure that the local community is involved and understands what energetik is, what it is trying to achieve and how this will benefit them
- Helping people to understand and manage their own energy use whilst assisting others to do the same encourages active citizenship
- The new homes that will be supplied will be more energy efficient, helping customers stay warm and well, and making people proud of where they live
- Public health will be improved through cleaner air and there will be no risk of carbon monoxide poisoning associated with gas boilers

8.3 Build our local economy to create a thriving place

8.3.1 The Council-owned energy Company will provide local benefits through jobs and employment opportunities as well as supporting a major boost to the local economy.

8.3.2 In addition, the Company's profits will eventually contribute to the Council's income, as it generates revenue and begins to accumulate retained earnings.

9. EQUALITIES IMPACT IMPLICATIONS

9.1 Due to the subject nature of this Report, there are no Equality Impact Implications. However, an EQIA Action Plan has been created and is regularly reviewed and updated.

10. PERFORMANCE AND DATA IMPLICATIONS

10.1 The Company reports to the Council regularly and will soon commence reporting to the Shareholder Committee.

11. HEALTH AND SAFETY IMPLICATIONS

11.1 The majority of energetik's works are carried out by sub-contractors. Contractors working for energetik are required under the terms of their agreements to manage health and safety (H&S) in accordance with all applicable law with respect to all works carried out.

11.2 The energetik management team has the responsibility to ensure it takes appropriate advice and carries out the required audits of contractors to ensure they are adhering to all H&S requirements. Energetik's project manager is responsible for the day to day management of this function and reports directly to the Technical Director. Both team members have approximately 30 years' experience delivering large scale construction projects in line with all H&S requirements.

12. HR IMPLICATIONS

12.1 Are not applicable at present as there are no employees.

13. PUBLIC HEALTH IMPLICATIONS

13.1 The delivery of energetik's Business Plan will create substantial carbon savings due to the avoidance of gas being installed across the heat networks. It is estimated that over the business plan, energetik will save over 230,000 tonnes of CO_2 (5,000 tonnes per annum average). Over the same period, 65 tonnes of harmful NOx will be avoided, which is the equivalent of taking 2,000 cars off the road each year.

Background Papers

None

Appendices

- **Appendix 1** - See Part 2 Report