

CABINET

8 JUNE 2021

RE:FIT PROGRAMME PUBLIC WORKS LOAN BOARD (PWLB)

Portfolio Holder: Councillor Adrian Gulvin, Portfolio Holder for Resources

Report from: Richard Hicks, Director of Place and Deputy Chief Executive

Author: Robert Dennis, Head of Property & Capital Projects

Summary

This report provides details of the Re:fit programme; a building retrofit and energy generation programme which will provide considerable revenue savings and deliver on the Council's Climate Emergency Declaration. This will be achieved by an 'invest to save' model where the Re:fit Framework contractor (Scottish and Southern Energy - SSE) will guarantee the savings. An outline business case for Re:fit as a whole and the Phase 1 detailed business case are presented here, with additional detail available in Exempt Appendix 1 and Appendices 2 to 3 of the report.

1. Budget and policy framework

- 1.1. The Cabinet is asked to recommend the addition of a total of £12 million worth of Public Works Loan Board (PWLB) funding to the Council's Capital Programme to help the Council to reduce its carbon footprint by delivering the Re:fit programme. Additions to the Capital Programme are ordinarily a matter for full Council.
- 1.2. The Re:fit Programme comprises a number of phases, with Phase 1 works due to commence this summer 2021. The business case for Phase 1 set out at Exempt Appendix 1 and Appendix 2 of the report indicates a maximum cost of £3.5m with minimum annual revenue savings of £274K.
- 1.3. The net revenue saving in year 1 is circa £14,000 after covering the annual cost of maintenance, monitoring of the savings and the loan repayments. This increases significantly in year four, when the Monitoring and Verification contract (M&V) ends. Over the estimated 20 year useful life of the assets, the Internal Rate of Return (IRR) calculation would mean that even at a discount rate of 7.5% the net cash flows would generate a positive Net Present Value

(NPV). However based on a more reasonable discount rate of 3.5% the NPV over twenty years works out at £1.643million

- 1.4. The savings are guaranteed by the contractor via Re:fit, which is a public sector Energy Performance Contracting Framework, so the risk is very low.
- 1.5. The carbon savings associated with Re:fit Phase 1 are 503 tonnes of carbon. In total, the programme is expected to deliver in excess of 2,000 tonnes of carbon savings. Re:fit is an integral part of the Climate Change Action Plan presented to the Climate Change Member Advisory Group on the 20 April 2021 and set out in this Cabinet agenda, agenda item 8, a key element of the Council's strategy to deliver on the Climate Change Emergency Declaration.
- 1.6. The next full Council meeting after Cabinet on 8 June 2021 is 22 July 2021. To wait to commence Phase 1 of the Re:fit Programme until after 22 July 2021 would delay the programme and risk some buildings not having heating in time for the heating season. Therefore, the Cabinet is asked to recommend that the Chief Executive uses urgency provisions as set out in paragraph 4.1. of the Employee Delegation Scheme (including consultation with the Leader of the Council and the Leader of the Labour Group) and adds the required funding for the first phase only to the Capital Programme (up to £3.5m). The use of these urgency provisions will be reported to Full Council on 22 July 2021 for information.
- 1.7. The Cabinet is also asked to recommend to full Council on 22 July 2021 that the remainder of the funding (up to £8.5m) be added to the Council's Capital Programme for Phases 2 to 4 of the Re:fit programme but this funding to only be released on receipt of a satisfactory business case (to be agreed by the Chief Finance Officer in consultation with the Leader of the Council).

2. Background

- 2.1. Utility costs are expected to double in next five to ten years, due both to mechanisms designed to aid the transition to Net Zero and more generally the trajectory of energy commodity prices continuing to rise. There is significant scope for improving the energy performance of Council buildings that are likely to be retained for the foreseeable future. By reducing costs, the proposed investment programme will help the Council to maximise the resources available to deliver essential services.
- 2.2. On February 2021, Medway Council appointed SSE as its energy partner following a mini-competition within the OJEU-compliant Re:fit Framework. The project had obtained Gateway 3 approval via Procurement Board in January.
- 2.3. Re:fit is an Energy Performance Contracting Framework, where the energy savings put forward are written into the contract and guaranteed by the contractor. This means that, should the project underperform, the contractor must remediate this at its own cost (e.g. adding additional energy saving projects) or pay the Council for the savings shortfall year on year until the shortfall has been addressed or the project has been fully paid back. The

Re:fit Framework also covers renewable energy projects where the performance guarantee is against the amount of green energy produced.

- 2.4. Re:fit has been named in the Climate Change Action Plan as the delivery mechanism for carbon and water savings in the corporate portfolio and sheltered housing. Council officers and the Re:fit team have already started working with Housing and Education services in order outline how they can reduce their energy consumption. This scheme will also support the development of renewable energy solutions for Medway Council, including solar and potentially wind and energy from waste.
- 2.5. Re:fit will focus on the reduction of the Council's energy consumption and its carbon footprint across a wide range of services, including offices, sports centres, depots, car parks and public conveniences.
- 2.6. To aid the Net Zero Carbon by 2050 commitment (and 78% by 2035, the new interim target), the Government has been making grant funding available to local authorities, especially for key items such a fleet electrification and heat decarbonisation.
- 2.7. These funding streams are often short-lived and have incredibly fast turnaround requirements. In addition, more often than not, they will only cover part of the cost of a project.
- 2.8. It is for this reason the full £12m is requested to be added to the Council's Capital Programme, to enable the Council to respond swiftly to these openings and benefit from the grant funding (as an example, the latest Public Sector Decarbonisation Fund was exhausted within days).

3. Options

- 3.1. Option 1: Do nothing – The Council will miss out on a low risk opportunity to achieve substantial revenue savings and leave the Climate Change Action Plan without a clear, tried and tested, delivery mechanism.
- 3.2. Option 2: Approve Phase 1 only and recommend the addition of up to £3.5m to the Capital Programme – The Council will get annual guaranteed revenue savings of £276K starting 2021-22 plus 503 tonnes of carbon saved every year. It will however potentially miss out on grant funding opportunities since projects that include partial Prudential Borrowing will have to be authorised at short notice and officers will not have the authority to do so.
- 3.3. Option 3: Approve the Re:fit programme, including business case for Phase 1 of the programme and recommend the addition of up to £12m to the Council's Capital Programme, as set out in section 1 of the report. In respect of Phases 2 to 4, funding to be subject to receipt of a satisfactory business case for each phase before any funds are released – The Council can reap the full benefits of the programme, including additional grant funding, but no borrowing will be authorised without a detailed business case.

4. Advice and analysis

- 4.1. The recommended option is Option 3.
- 4.2. The Cabinet is advised to agree Option 3 and, in so doing, agree to delegate authority to the Director of Place and Deputy Chief Executive, in consultation with the Portfolio Holder for Resources, to deliver the programme. This represents a very low risk 'invest to save' opportunity since the savings are guaranteed by the contractor, plus it provides carbon savings.
- 4.3. The Cabinet is asked to recommend that the Chief Executive, using urgency powers, agrees to add up to £3.5m to the Council's Capital Programme, funded from Prudential Borrowing, to deliver the first phase of the Re:fit programme. This is so that the programme can be delivered in a timely manner that will ensure continuity of service, e.g. without affecting heating to occupied buildings.
- 4.4. The Cabinet is also asked to recommend to full Council on 22 July 2021, the addition of up to £8.5 million to the Council's Capital Programme, funded from Prudential Borrowing, to deliver phases 2 to 4 of the Re:fit programme. This is so that officers can bid for grant funding that requires blended finance and needs a quick turnaround. It also gives the Climate Change Action Plan some resilience by giving officers the opportunity to budget for several phases.
- 4.5. Due consideration has been given to the sustainability of this initiative. Not only does it support the Council's Climate Change agenda, but it does so in a tried and tested manner that provides a low risk delivery mechanism. The Re:fit Framework has been delivering this kind of project for over a decade and it is one of the few Energy Performance Contracting Frameworks in the country. In addition, any additional revenue savings above and beyond what the contractor achieves will remain with the Council and can help bolster future Re:fit phases or any other Council needs.
- 4.6. This report does not recommend any policy/service changes, merely the addition of funding to the Capital Programme. In addition, improvement works on Council buildings will benefit all employees and visiting members of the public in an equal manner, same as carbon reductions. For this reason a Diversity Impact Assessment (DIA) has not been completed.

5. Risk management

Risk	Description	Action to avoid or mitigate risk	Risk rating
The investment does not pay off	The Council borrows money but the savings (financial or carbon) do not materialise	By using the Re:fit Framework the Council eliminates this risk since the savings are guaranteed by the contractor. Having	F2

Risk	Description	Action to avoid or mitigate risk	Risk rating
		this guarantee written into the contract is the cornerstone of the Re:fit Framework.	
Cost overrun	Scope creep and predicted costs make the total capital cost go up	All Re:fit projects have Defined Performance Parameters written into the contract. These include maximum cost and minimum savings meaning SSE cannot go beyond the £3.5m for this Phase 1 unless additional projects are identified that deliver additional savings.	F2
Delays cause disruption	Re:fit works will be taking place in occupied buildings and affect key building services. Delays could disrupt employees and/or Council services	The Capital Programme team has chosen a tried and tested Framework and a seasoned contractor. Liquidated Damages will be part of the contract and the team is trying to secure timely approvals to ensure the heating works finish before the heating season starts.	E3

6. Consultation

- 6.1. Officers have consulted with the Portfolio Holder for Resources and the Deputy Leader and Portfolio Holder for Housing and Community Services about the kind of projects Re:fit brings with it and how to present the financial information. Re:fit has been well received.
- 6.2. Re:fit is a firm step towards a Green Recovery after the pandemic, delivering much needed revenue savings and diversifying income. In addition, Re:fit is

an integral part of the Council's Climate Change Action Plan and will deliver a reduction of an estimated total of 2,047 tonnes of carbon over 4 phases.

7. Climate change implications

- 7.1. [The Council declared a climate change emergency in April 2019](#) and has set a target for Medway to become carbon neutral by 2050.
- 7.2. All Council officers have a responsibility to take action to reduce the carbon footprint associated with the services they provide. Re:fit is the vehicle chosen by the Capital Programme team, who aim to lead by example in contributing large amounts of carbon savings towards this target.

8. Financial implications

- 8.1. The cost of utilities for the Council's portfolio is in the region of £4.5m per annum (£0.5m on water, which Re:fit can also tackle). The buildings on Phase 1 alone use £0.8m worth of gas and electricity per year. Re:fit Phase 1's annual savings of a minimum of £276K represent a revenue saving of 35%.
- 8.2. The contractor is committed to deliver a minimum of 20% savings on revenue cost on each subsequent Re:fit phase with the cost for the entire corporate portfolio estimated at £12m. This figure is based on a central scenario of savings (see Appendix 3) and replacing gas boilers with low carbon heating only in half of the estate (If the Council wanted to replace all gas boilers with heat pumps the total cost of the programme will be £12.7).
- 8.3. The cost of borrowing has also been included in the calculations for an extended term of 20 years (so that the Council can have a more cash positive investment profile).
- 8.4. The stated N.P.V. includes the Council measuring and verifying the savings for a period of 3 years after the completion of the Works (Measurement and Verification – M&V is a feature of any Energy Performance Contract as it is the mechanism used to ensure the contractor has delivered on the promised savings).
- 8.5. In addition to the revenue savings at Appendix 2, this Re:fit Phase 1 will be addressing circa £700K of backlog maintenance works as identified by Medway Norse. These items are being addressed as part of the improvements planned by SSE, which allows both funds and man-hours to be reallocated to other pressing matters.

9. Legal implications

- 9.1. Local Authorities are able to access long-term, low cost loans via the Public Works Loan Board (PWLB) managed by HM Treasury. In addition, Section 1 of the Local Government Act 2003 grants Local Authorities the general power to borrow money for any purpose relevant to its functions under any enactment.

- 9.2. The Council entered into a Contract with SSE on 18 February 2021 for the provision of services ancillary to the Re:fit Framework. The Contract governs the overarching relationship between the two parties and provides the Council with a number of legal protections and options including a voluntary termination provision should it no longer wish to proceed with the Re:fit programme.
- 9.3. The Contract between the Council and SSE provides for a 'Savings Guarantee', meaning the Local Authority has legal recourse via the Contract in the event that any energy savings that have been guaranteed by SSE are not met.
- 9.4. Members should also bear in mind the legal, financial and reputational implications to the Council in the event that the Council defaults on its payments for whatever reason.

10. Recommendations

- 10.1. The Cabinet is asked to agree Option 3 as set out paragraph 3.3 of the report and in doing so:
- i) approve the Re:fit programme, including the business case for phase 1 of the programme as set out at Exempt Appendix 1 and Appendix 2 of the report;
 - ii) agree to delegate authority to the Director of Place and Deputy Chief Executive, in consultation with the Portfolio Holder for Resources, to deliver the Re:fit programme, including the submission of bids for grant funding if and where necessary;
 - iii) agree to delegate authority to the Chief Finance Officer, in consultation with the Leader of the Council, to approve the business case for each further phase of the Re:fit programme (phases 2-4) and agree to release the required funding.
- 10.2. The Cabinet is asked to recommend that the Chief Executive, using urgency powers (in place of referring this matter to full Council), agrees to add up to £3.5m to the Council's Capital Programme, funded from Prudential Borrowing to deliver the first phase only of the Re:fit programme.
- 10.3. The Cabinet is asked to recommend to full Council on 22 July 2021 to agree the addition of up to £8.5 million to the Council's Capital Programme, funded from Prudential Borrowing to deliver phases 2 to 4 of the Re:fit programme.
- ## 11. Suggested reasons for decisions
- 11.1. To provide revenue savings and carbon reduction, to provide a delivery vehicle for the works associated with the Climate Emergency in council stock (including HSA and schools), to be ready to apply for carbon reduction grant funding.

Lead officer contact

Rob Dennis, Head of Capital Projects
Telephone: 01634 332880
Email: rob.dennis@medway.gov.uk

Appendices

Exempt Appendix 1 - Re:fit Phase 1 Business Case
Appendix 2 - Re:fit Phase 1 Discounted Cashflow
Appendix 3 - Re:fit Phases 2 to 4 Budgeting based on Medway Buildings Data

Background papers

[Medway Net Zero Carbon – Baseline and Pathway Technical Report](#)