

	<p align="center"><b>London Borough of Hammersmith &amp; Fulham</b></p> <p align="center"><b>CABINET</b></p> <p align="center"><b>7 SEPTEMBER 2015</b></p>
<p align="center"><b>PROCUREMENT OF ENERGY - FLEXIBLE 2016 – 2020 AND FTFP 2016 – 2018</b></p>	
<p align="center"><b>Report of the Cabinet Member for Finance – Councillor Max Schmid</b></p>	
<p><b>OPEN REPORT</b></p> <p>A separate report on the exempt part of the Cabinet agenda provides exempt financial Information.</p>	
<p><b>Classification – For Information</b>  <b>Key Decision: Yes</b></p>	
<p><b>Wards Affected:</b> All</p>	
<p><b>Accountable Executive Director:</b> Nigel Pallace, Chief Executive</p>	
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## 1.0 EXECUTIVE SUMMARY

- 1.1. This report details the energy contract currently held by the Council for periods 2012-2016 with LASER. It also details procurement proposals for 2016-2020 when they next become due for renewal.
- 1.2. An energy procurement frameworks review was carried out between 2011-2014 by the London Councils' public sector collaboration, London Energy project (LEP). LASER was evaluated as achieving good performance against the market benchmark meaning it still achieved a good "Value for Money" savings for both gas and electricity. Also their flexible, risk managed procurement was still proven to be effective in controlling commodity costs and continues to be the most appropriate price risk management strategy currently available for the council.

- 1.3. Existing supplies covered by the current 4 year Laser Flexible Purchasing arrangement are suitable for transfer to the new framework that will come into effect in October 2016. It is also recommended that supplies identified as suitable for fully managed flexible purchasing that currently sit under the FTFP and Flex Light contracts are transferred to the new framework in October 2016 when their current contracts end.
- 1.4. After careful consideration of risks and benefits involved, it is recommended that the council considers staying with PIA (Purchase in Advance) for all electrical procurement but switch to PWP (Purchase within Period) for gas as officers believe further savings are possible due to the consistent volatility and drop in gas and oil prices.
- 1.5. Supplies which are not suitable (uneconomic) for transfer to flexible contracts will be subject to a separate procurement exercise through Laser under the FTFP tender framework, in order to achieve the best price and ensure compliance with OJEU and public sector procurement regulations. A FTFP contract would run for two years from October 2016 with provision for a one year extension.

## **2.0 RECOMMENDATIONS**

- 2.1 To waive the provisions of Contract Standing Orders in relation to authority to award energy contracts.
- 2.2 To delegate to the Director of Finance and the Director for Building & Property Management the authority to enter into contracts with utility companies following the competitive procurement exercises via a Central Purchasing Body (currently LASER operated by Kent County Council) to take effect from October 2016 for 4 years. The procurement for the new framework has been carried out in accordance with EU procurement regulation.
- 2.3 For Members to receive an annual report on the contracts let by officers and proposals concerning the procurement of energy by the Council for the following year.

## **3.0 REASONS FOR CONTINUED ENERGY PROCUREMENT THROUGH LASER**

- 3.1 Flexible Procurement managed by an approved Public Sector organisation is recommended for all public bodies by the PAN Government Energy Review Project (part of the Cabinet Office). The project has produced a number of reports supporting the adaptation. In addition the Green Report on public sector purchasing identified Energy as the only category where public sector achieved leverage through aggregations, achieving best value.
- 3.2 Flexible contracts are where the council's energy consumption requirements are aggregated and the energy commodity is risk managed within the wholesale market by specialist energy buying organisations. The energy supplier declares its cost to serve through a competitive tender process and the regulated (by government) fees are passed through in a transparent way. The supply framework normally lasts for four years but the contract prices are adjusted

annually to recover the raw (tradable) energy cost and the actual cost of regulated fees and charges.

- 3.3 The procurement of energy via a central purchasing body (CPB), amongst many advantages, saves the council money based upon the buying power. Laser which has been used by the council since 2008, purchase on behalf of over 120 Local Authorities and Universities and has demonstrated great efficiencies over the years. LASER is a “not for profit” energy buying group operated by Kent County Council.
- 3.4 The use of LASER as a Central Purchasing Body complies with the requirements of the Public Contract Regulations 2015. Given the expertise of the LASER organisation it is seen as the most effective, efficient and economical way for the Council to procure its energy requirements.
- 3.5 An energy procurement frameworks review was carried out between 2011-2014 for LBHF by the London Councils’ public sector collaboration, London Energy project (LEP). LASER was evaluated as achieving good performance against the market benchmark meaning it still achieved a good “Value for Money” savings for both gas and electricity. Also their flexible, risk managed procurement was effective in controlling commodity costs and continues to be the most appropriate price risk management strategy currently available for the councils.
- 3.6 The use of LASER as the council’s CPB provides OJEU compliant framework contacts for energy procurement as well as providing a number of other benefits including:
- Reduction in cost or energy procurement by negating need to manage individual OJEU processes
  - Support for dispute resolution with suppliers
  - Specialist energy procurement and management skills
  - Continuity of skills
  - Value added services (e.g. bureau services, energy demand reduction services, AMR installation services)
  - Leverage with suppliers

#### **4.0 INTRODUCTION AND BACKGROUND**

- 4.1 The public sector spends billions of pounds each year in a volatile market that is also set for price increase in energy costs. Energy is often a high profile spend category due to extreme price hikes; prices can fluctuate up to 5% on any given day and up to 100% in a year.
- 4.2 Flexible purchasing allows for the price of raw energy to be fixed over a number of trades on the wholesale market. There are a number of benefits to the use of flexible purchasing when compared with other methods of procurement and these are:
- Transparency over all costs that make up energy charges
  - Focus on controllable energy cost element
  - Purchasing conducted in real-time
  - No long-term price lock in

- Reduced forward risk premium
- Responsive to market trends
- Managed supplier transfers

- 4.3 The monitoring of energy consumption and payments for buildings covered by these contracts is undertaken by Professional Services Team within Transport and Technical Services, for corporate sites and the Estate Services Utilities Team within the Housing Department for Council Housing, both teams now utilising an external agency service provided by LASER Bureau Service.
- 4.4 The Laser Bureau Service allows the investigation of any abnormal consumption against targeted consumption over the previous twelve months. Working closely with their Bureau who validate bills prior to payment and using the now centralised finance system for dealing with utility bills result in reducing energy usage and costs.
- 4.5 Analysis of energy supply usage and consumption on a site by site basis also allows the site supply to be placed on the most appropriate and cost effective contract or flexible purchasing framework.
- 4.6 The use of LASER's Bureau also assisted the council to provide energy use data under the Carbon Reduction Commitment Energy Efficiency Scheme (CRC EES) obligations as required from April 2010. It should also be noted that due to the success of the framework, it was one of the key elements which attributed the Council to no longer qualify for CRC Phase 2 reporting as consumption has dropped below the required threshold.
- 4.7 STARK has been chosen as a supplier for Automatic Meter Readers (AMR) and phase 1 of the AMR roll out is now complete. Npower, one of the council's electricity suppliers which are managed by LASER will also be carrying out AMR roll out for a number of council sites to allow the Professional Services Team and Housing Department Utilities team to best monitor electricity use.
- 4.8 The proposed frameworks are compatible with the housing department's strategy for reducing energy consumption, costs and carbon footprint. The housing department is assessing the benefits of setting up Combined Heat and Power (CHP) or Cogeneration schemes on housing owned land or co-located with housing estates where appropriate. The CHP process captures and uses heat that is a by-product of the electricity generation process. The heat generated during this process is supplied to an appropriately matched heat demand that would otherwise be met by a conventional boiler
- 4.9 The advantages of CHP include an efficiency rate of over 80%; users typically save around 20% on energy bills for schemes put into operation; transmission and distribution losses are reduced and fuel supply security is increased. By generating heat and power simultaneously, CHP can reduce carbon emissions by up to 30% compared to conventional generation

## 5.0 CONTRACT PROPOSAL FOR PROCUREMENT OF ENERGY FROM OCTOBER 2016 to SEPTEMBER 2020

5.1 As set out in the exempt report on the exempt Cabinet agenda.

## 6.0 OPTIONS ADOPTED ISSUES

6.1 LASER are now requesting that the Council o enter into the contracts to join the 2016-2020 framework. The contracts are in a form of Tripartite agreements between the LBHF (customer), the supplier and Kent County Council (the Purchaser).

6.2 The following baskets are available under the Flexible Risk Managed options:

6.2.1 **Purchase in Advance (PIA)** - Purchases are completed in advance of the contract year. Supplier cost-to-serve fixed in the contract. The timing of purchases is at LASER's discretion, in conjunction with parameters set by the Governance Panel. Fixed prices for the contract year are advised to the customer prior to opening bills being issued.

6.2.2 **Purchase within Period (PWP)** - Purchases are completed in advance and within each 6 month contract period. Supplier cost-to-serve fixed in the contract. The timing of purchases is at LASER's discretion, in conjunction with parameters set by the Governance Panel. A reference price is applied on invoicing, with a reconciliation occurring at the end of each 6 month period between the reference price and the final achieved price.

6.2.3 **Flexible Light** - Purchases are completed in advance of the contract year. Supplier cost-to-serve fixed in the contract. LASER purchases energy requirements at its discretion in several blocks.

6.3 The process for the flexible procurement of energy via LASER requires a minimum agreement for a four year period to be viable. The council has been using the chosen basket PIA which has so far been deemed suitable for the past market trends within the gas and electric market. It is recommended that the council considers staying with PIA for all electrical needs due to economic stability but switch to PWP for gas as officers believe further savings are possible due to the consistent volatility and drop in gas and oil prices. PWP are good for large gas supplies needed throughout the property portfolio, as the PWP option has usually achieved a lower price than the Locked option PIA. This is particularly relevant where 'actual' consumption data such as advanced metering exists. Prices are concluded for each supply year commencing 1<sup>st</sup> of October to 30<sup>th</sup> of September the following year and contracts are drawn for 4 years.

6.4 The council will continue to choose between relevant baskets PIA and PWP as this is identified as the best solution for flexible procurement for the council needs. The contract basket arrangements will remain under close scrutiny over the duration of the contract and it will be feasible to swop from PWP to PIA and vice versa if that basket is found not to be any longer an economically viable option during the 4 year term provided a 6 Month notice is given to LASER if the

council wishes to make any amendments to their chosen baskets once the contract commences.

- 6.5 **Fixed Term Fixed Price (FTFP)** - Not all metered electricity supplies are suitable for transfer to a flexible purchasing arrangement due to the higher management costs incurred with flexible purchasing of energy supplies. Flexible purchasing arrangements are most suitable for larger supplies where savings realised through flexible purchasing will more than offset the increased management costs. For smaller supplies it is more cost effective to procure supplies through a FTFP contract.

## 7.0 OPTIONS AND ANALYSIS OF OPTIONS

- 7.1 Given current good levels of performance with aggregated, flexible, risk managed energy contracts, having OJEU compliant procurement methods and the degree of transparency offered around buying performance, fees and other charges. It is recommended that the council continue using aggregated, flexible, risk managed energy contracts as provided by LASER i.e. to engage a strategic risk managed approach that delivers overall best performance, as a means of achieving value for money as part of their wider energy strategy.
- 7.2 To date the buying and risk management of LASER has been good with LASER delivering achieved prices that were below market average. The London Energy Project has evaluated the aggregated flexible, risk managed contracts provided by LASER and recommends their use at contract renewal.
- 7.3 As per recommendations the council will sign the tripartite agreements and commit to LASER – PIA flexible contract framework for the framework period of October 2016- September 2020. For PWP basket energy prices are concluded prior to and within the supply periods (October- March and April- September. 6 Months' notice should be given to LASER if the council wishes to make any amendments to their chosen baskets.
- 7.4 Reviewing previous reports and recommendations the council will choose the PIA basket option for electric and PWP basket option for gas as this is identified as the best solution for flexible procurement for the council needs after careful consideration of risks and benefits involved. The Professional Services Team and Housing Utilities Team worked closely with LEP who carried out an Energy Strategy Review for LBHF and assessed the way that the council has been procuring energy through LASER.
- 7.5 It is noted that the council will continue to purchase gas and electricity through a framework set up by a central purchasing body. This procurement approach is in accordance with EU procurement rules and the Council's contract standing orders.
- 7.6 The Housing Department is currently carrying out a stock options appraisal that may result in a transfer of housing stock. Corporate and Housing supplies will be set out separately within the contract and provision agreed for the contract to be formally split and housing sites novated to a new legal entity should the

requirement arise following the completion of the stock options appraisal and any decisions arising from its recommendations.

## **8.0 CONSULTATION**

- 8.1 Both departments (HRD and T&TS) have been consulted with regards to a joint report submission.
- 8.2 Leaseholders will have to be formally consulted before the contract can be entered into. This process usually requires two notices to be issued: a Notice of Intention and a Notice of Proposal. A Notice of Intention to enter into a new agreement for the provision of gas and electricity can be served as soon as required on the leaseholders who benefit from the services. Officers will however not be able to serve a Notice of Proposal allowing leaseholders the statutory 30 days to make observations before we enter into the agreement, as the required information will not be available. This is due to the nature of the procurement; a quote has to be accepted immediately and because of the continuous buying cycle the prices are only known at the end. We will therefore have to approach the First-tier Tribunal applying for a dispensation of the consultation regulations.
- 8.3 Leaseholders will be advised of the application and will be able to make comments as part of the process or make a case as respondents.
- 8.4 The Council was granted similar dispensation in 2012.

## **9.0 EQUALITY IMPLICATIONS**

- 9.1 There are no specific equality implications related the contact requirements and consequently an Equality Impact Assessment has not been produced for this report.
- 9.2 Implications verified/completed by: Sebastian Mazurczak, Professional Services, x1707.

## **10.0 LEGAL IMPLICATIONS**

- 10.1 Using LASER Energy Buying Group as a central purchasing body as defined in Regulation 2 of the Public Contract Regulations 2015 to procure the council's gas and electricity supplies meets all legislative requirements.
- 10.2 Implications verified/completed by: (Babul Mukherjee, Solicitor (Contracts), 020 7351 3410).
- 10.3 Housing Implications verified/completed by: (Jana Du Preez, Leasehold Services, 020 8753 4242).

## **11.0 FINANCIAL AND RESOURCES IMPLICATIONS**

- 11.1 The recommendation is for the tripartite agreements with LASER for a four-year contract period from # October 2016 to # September 2020. The preferred option for the procurement of electricity is the 'Purchase in Advance' method and 'Purchase within Period' for Gas. The 'Purchase within Period' option is more suitable for gas due to the volatility of gas and oil prices.
- 11.2 The Flexible contract allows the council to continue using aggregated, flexible, risk managed energy contracts as provided by LASER. This will allow for a strategic risk managed approach that delivers overall best performance as a means of achieving value for money as part of the wider energy strategy.
- 11.3 The contract arrangements will remain under scrutiny by the Professional Services and Housing Team over the duration of the contract and it will be possible to change from PWP to PIA and vice versa depending on the economic viability of each option during the 4 year term.
- 11.4 Implications verified/completed by: Gary Hannaway, Head of Finance – TTS – 020 8753 6071.

## **12.0 IMPLICATIONS FOR BUSINESSES**

- 12.1 There are implications for businesses as the contract covers all council assets namely corporate buildings, housing and street lighting. These will be managed by the LASER contract and the Professional Services Team.
- 12.2 By entering into this procurement for the provision of energy it will not prevent the Council from producing its own supply in the future if it wished.
- 12.3 The Council needs to explore further the inclusion of small businesses or other commercial businesses in the Laser contract.
- 12.4 Implications verified/completed by: Sebastian Mazurczak, Professional Services, x1707

## **13.0 RISK MANAGEMENT**

- 13.1. The Shared Services Risk Manager agrees with the recommendation that the council continue using aggregated, flexible, risk managed energy contracts as provided by LASER and to engage a strategic risk managed approach that delivers overall best performance, as a means of achieving value for money as part of their wider energy strategy. This contributes positively to the management of Market Risk and Market Testing as noted in the Shared Services Risk Register, Risk number 4 delivering high quality commissioned services that are at best cost to the local taxpayer.



13.2. Performance management of the contract shall remain the responsibility of the Transport and Technical Services Department. Further savings from the new strategy would contribute to savings through smarter procurement thus contributing positively to the management of risks 1 and 2 managing budgets and the effect on LBHF of reductions in grants from central government.

13.3. Implications verified by: Michael Sloniowski, Risk Manager 020 8753 2587

#### **14.0 PROCUREMENT AND IT STRATEGY IMPLICATIONS**

14.1 Contract Standing Order 22 provides delegated powers to officers to award energy related contracts on behalf of the Council and to provide an Information Report to the Cabinet on their decision

14.2. The use of LASER Energy Buying Group (the trading arm of Kent County Council acting as a Central Purchasing Body) meets legislative requirements.

14.3. Implications verified/completed by: Alan Parry, Procurement Consultant (TTS) – 020 8753 2581.

#### **LOCAL GOVERNMENT ACT 2000** **LIST OF BACKGROUND PAPERS USED IN PREPARING THIS REPORT**

<b>No.</b>	<b>Description of Background Papers</b>	<b>Name/Ext of holder of file/copy</b>	<b>Department/ Location</b>
1.	Previous Cabinet and Committee reports on energy procurement (published)	Sebastian Mazurczak x1707	Professional Services, TTS – 5 <sup>th</sup> Floor HTHX
2	LASER – Energy Buying Group: <i>Flexible Energy Frameworks 2016 – 2020 Information Pack (exempt)</i>	Sebastian Mazurczak x1707	Professional Services, TTS – 5 <sup>th</sup> Floor HTHX
3	London Energy Projects: <i>Energy Contracts Value for Money Assessment 2011-2014 (exempt)</i>	Sebastian Mazurczak x1707	Professional Services, TTS – 5 <sup>th</sup> Floor HTHX

**LIST OF APPENDICES: None**