

2022 12 06 Establishing the City Leap Energy Partnership – Appendix G – Financial Advice

Background

1. Following the successful procurement to appoint a Strategic Partner (SP) and approval by Cabinet in April 2022 to appoint Ameresco / Vattenfall as the Preferred Bidder, following a six-month mobilisation phase, where all parties have worked collaboratively, the Authority now plans to enter into a Concession Agreement with the SP for a term of 20 years to implement low carbon energy infrastructure technologies and exploit the wider opportunities across the Council's estate and wider Bristol community.
2. As part of the procurement, and as approved by Cabinet in July 2022, the Council's Heat Network Assets (HNA) will transfer to Bristol Heat Networks (BHNL), the Council's wholly owned company, which will be acquired by Vattenfall under the terms of the Share Purchase Agreement (SPA).
3. A Joint Venture company (JVCo) will be established between the parties (Ameresco and Bristol City Council), and which will focus primarily on project origination to deliver the SP's business plan.
4. The value of the assets to be transferred is set out below, and the purchase consideration is based on the level of debt owed to the Council by BHNL at the point of transfer, predominantly arising as a result of the Asset Transfer and working capital requirements of the company. The share consideration will be £1.
5. Following a successful period of consultation with the Energy Services staff, most of the existing workforce will transfer to the City Leap Joint Venture Company under TUPE, with a small team remaining with the Council to manage the Council's energy budget and non-heat network assets.
6. A new Client function is intended to be created, which will be a key interface between the Strategic Partner and the Council, with its primary aim to effectively manage the relationship, facilitate delivery of the business plan in accordance with the terms of the Concession Agreement, monitor the Strategic Partner's performance to ensure that maximum value is delivered for all stakeholders and customers and ensuring that the latest technologies/ innovative solutions are deployed to deliver the City Leap outcomes.
7. As part of the requirements of the Invitation to Tender (ITT) Bidders were asked to submit three pricing elements, in addition to the payment for the HNA via the acquisition of BHNL:
 - a. The Concession payments are guaranteed payments, albeit variable across the 20-year timeframe.
 - b. The Authority Share Payments are not guaranteed and are based on a revenue share formula (% of capital deployed in relation to non-heat assets and new connections on the Heat Networks).
 - c. No Authority Contribution to JVCo was sought by the Preferred Bidder (PB).
8. The phasing of these payments over the initial five-year period is set out in the CBA in Annex A and has been updated for refreshed Initial Business Plan (see Appendix A (ii)).

Financial Assessment

9. As part of the Report to grant the twenty-year concession to the Preferred Bidder, to be presented to Cabinet on 6 December 2022 and to aid in that decision, the following high-level Financial Assessment of the overall Cost-Benefit to the Authority has been set out, alongside key financial highlights of the SP's Initial Business Plan (see Exempt Appendix I (i)).
10. The timeframe for the analysis is a five-year period, commencing Financial Year 22-23
11. The financial analysis and tables set out within this document is based on available data, some of which is evolving and therefore should be considered at a "Draft" status.
12. In arriving at the overall cost-benefit analysis (CBA), certain assumptions and varying degrees of judgement have been used. The underlying cost base is reasonably understood, however areas such as the Heat Model future income generation, which remains subject to current pressures and volatility on utility costs, inflation, and financing costs should be considered indicative only. This is not considered to have a material impact on the overall CBA as the assumptions are largely consistent with previous analysis undertaken and is therefore excluded from the CBA.
13. All figures are presented in 2022 values with the HM Treasury discount rate of 3.5% + inflation at 5% (nominal) used to calculate a Net Present Value (NPV)
14. Costs to date in procuring the City Leap Partner are a sunk cost and are deemed not relevant to the decision and therefore only noted in this report for completeness.
15. Other than non-guaranteed Income to the Authority, no adjustment has been made for optimism bias, on the basis that the figures are Indicative and are presented based on a reasonable level of analysis of data submitted by the Preferred Bidder, and existing financial models maintained by the Authority.
16. Budget data for the financial year 22-23 is used to capture indicative financial benefit to the Council arising from the transfer of staff and related activities to JVCo. This may not be reflective of the current cost base as for example it excludes recent 22-23 pay awards which are averaging at 6.2% for the Council.
17. The overall cost and re-charging of utility costs, remains the responsibility of the Council and will be managed by the remaining Energy Services staff. These costs are not relevant to this decision and are therefore not included in this assessment.
18. The CBA excludes any specific risks noted elsewhere within the documents, specifically Appendix D (Risk Assessment), and Appendix H (Legal Commentary), though any quantifiable indemnities are included, noting final agreement has yet to be reached as part of finalising the suite of legal agreements.
19. The wider economic benefits and carbon emission reductions are not addressed as part of the financial assessment and commentary, though overall Co2 savings are noted, as set out in the SP's Initial Business Plan.
20. The Initial Business Plan submitted by the Preferred Bidder and to be appended to the Concession Agreement is subject to a separate summary and is only shown here as an aide memoire and is not assessed as part of this commentary.

Preferred Bidder Revised Business Plan (BP) highlights

21. An Initial Business Plan has been submitted by the Preferred Bidder, segregated between Non Heat Assets (deployment of low carbon energy infrastructure assets, the responsibility of Ameresco) and the build out and operation of the Heat Network via BHNL being acquired by Vattenfall.
22. The Initial Business Plan shows an acceleration in the rollout of infrastructure across the Council's estate, though the funding arrangements, including the use of further grant income, has yet to be determined.
23. A list of identified Projects on the council's estate is included within the Initial Business Plan, noting sources of funding have yet to be secured and Project Acceptance Criteria (PAC) met to enable proposals to proceed.
24. The Initial Business Plan also shows an acceleration of capital investment in the Heat Networks.
25. It should be reiterated that the Council is not seeking approval for new council capital funding for City Leap projects in delivery of the Initial Business Plan appended to this Cabinet Report and as such should be considered an illustration only. Any and all future capital funding contributions made by the Council to City Leap projects will be subject to the usual decision-making and scrutiny processes of the Council.
26. See Exempt Appendix (i) – Detailed Financial Commentary for a detailed analysis of the Initial Business Plan.

City Leap Project Budget

27. The City Leap Project Forecast from inception is set out below and shows that forecasted expenditure is expected to be contained within the approved budget envelope to December 2022.
28. However, additional external advisors' fees of circa £180k over and above previously approved levels will likely be incurred by this date, requiring formal extension and approval in line with the Council's procurement rules. These sums are included in the forecast.
29. As there will be a requirement to conduct final reconciliations and prepare Completion Accounts post the completion date, the identified contingency of £56k will be used for this purpose, with any additional spending requirements funded via other savings arising as a result of the transaction.

City Leap Budget - £k	Procurement Phase	Mobilisation Phase *	Total
Core team - BCC staff	713	187	900
Core team - Agency	459	8	468
Core team - Internal professionals	1,473	655	2,129
External Advisors - Financial	1,147	209	1,356
External Advisors - Legal	1,369	232	1,601
Client Function mobilisation	42	198	240
External Advisors - Commercial energy	694	-	694
Marketing & Travel	141	25	166
Internal recharges - other	12	230	242
Energy innovation services	1,187	-	1,187
Contingency		56	56
TOTAL	7,238	1,800	9,038

** To 31 December 2022*

The Council's Energy Service's (ES) Budget

30. The Council's Energy Service's Budget comprises both Revenue and Capital items. The assets include Heat Networks, Wind Farm, Solar Park, Rooftop PV and Biomass Boilers.
31. Only the Heat Network assets will transfer to BHNL, as approved in the July 2022 Cabinet report.
32. The existing ES team manages all low carbon energy assets, alongside managing the Council's overall utility costs, including some schools.
33. An analysis of the ES Revenue Budget 22-23 has been provided to determine the underlying cost base and revenue streams, both pre and post City Leap.
34. Under the terms of the Concession Agreement most of the ES team will transfer to the Joint Venture Company, with a small team remaining with the Council to manage the Council's non Heat Network Assets and utility costs.
35. The current number of employees is 33 of which 27 will transfer under TUPE.
36. It is anticipated that all associated costs of the client function will be contained within the resulting base budgets for the ES service post transfer to city leap and it should be noted that there is no growth provision for the Client Function in the current medium term financial planning assumptions.
37. The Client Function Budget is currently being worked-up and indicative costs through to 31 March 2023 amount to circa £260k. A number of posts will be created and the annualised costs are reflected within the £378k outlined in the table below.

The ES Revenue Budget

Service Budget £k		Pre-Transfer	BCC	Client Function	City Leap
Category					
1	Employees	2,399	293	378	1,728
2	Premises-Related Expenditure	6,997	6,922	-	75
3	Transport-Related Expenditure	1	1	-	-
4	Supplies & Services	349	349	-	-
5	Third Party Payments	250	250	-	-
7	Support Services	237	137	-	100
8	Depreciation and Impairment Losses	(471)	(471)	-	-
9B	Income - Other Grants/Reimbursements and Contributions	(265)	(10)	-	(255)
9C	Income - Customer and Client Receipts	(4,866)	(4,646)	-	(220)
9E	Income - Recharges	(4,238)	(2,814)	-	(1,292)
X	Capital Financing Costs	744	744	-	-
Net Total		1,137	755	378	136
Total					514

The ES Capital Budget

38. The Council's current ES Capital Budget is shown below, together with the main sources of funding.

39. The level of approved PWLB borrowing is £22.7m, and as noted in the July 2022 Cabinet report, the estimated funding requirement to 31 December 2022 was £24m. The Heat Network Budget has been revised accordingly with the additional £1.3m being funded from the Council's Capital Contingency Budget.

40. An overspend of £2.3m is forecast against Old Market, Redcliffe and PSDS programmes and it is anticipated that this additional spend will be absorbed by a slower rate of spend on Bedminster, though this is a timing issue only and would have to be addressed if the appointment of the SP did not proceed.

Scheme	Budget / Forecast £k				Funding Sources £k			
	Budget	Spend to date (P7)	Forecast to Mar 2023	Variance	PWLB	Grant	Connection Fees	Total
Redcliffe Phase 2 & Old Market	26,300	26,000	27,600	(1,300)	12,597	10,159	3,544	26,300
Bedminster	11,685	3,961	6,800	4,885	5,707	1,348	4,630	11,685
Temple *	1,796	539	-	1,796	-	1,796	-	1,796
PSDS	6,900	7,000	7,900	(1,000)	-	6,938	-	6,938
Phase 1 - Assets transferring	6,663	6,663	6,663	-	4,438	2,226	-	6,663
Total	53,344	44,163	48,963	4,381	22,742	22,467	8,174	53,382

* Commercialisation Phase only

41. The analysis undertaken of historic assets identified that up to £500k may be attributed to initial feasibility studies for the initial phases of the city centre heat network, for which no physical asset exists. This will therefore need to be reversed from capital (revenue reversion) and a charge will need to be made to the revenue budget funded by general reserves.

Pension Obligations for Transferring Employees

42. The new employer assumes the ongoing financial responsibility to provide the pension benefits under the Local Government Pension Scheme in respect of those employees in the fund whose employments transfer (note the fund will be closed to new employees). Any pension liabilities accrued prior to the

start of the agreement will not be charged to the new employer and as such the new employer commences on a '100%' funded status on inception. Previous estimate provided by the Avon Pension Fund estimated the value of the fund to be £2.864m as at the 31 March 2021. This will be matched by assets of the same value being transferred from BCC's fund in APF to City Leap's fund in APF, this way City Leap commences with no deficit and any variation will be subsumed into BCC's fund. As the contract progresses, a surplus or deficit may emerge and this will be managed at triennial valuations.

43. The Council will require the City Leap entity to guarantee the liability in respect of all amounts due from it and protect the fund against any identified risks. The potential funding risks and guarantee / bond requirement was assessed with an initial value of c.£0.190m. The guarantee will only become valid if the admitted body ceased to exist (if they went into liquidation, for example) and the Fund will attempt all possible ways of receiving any deficit from the admitted body first.
44. The triennial valuation is currently underway following conclusion of which the calculations will be updated to reflect current market conditions and changes in underlying assumptions. As such the figure above are subject to change.

Contingent Liabilities

45. Under the terms of the Share Purchase Agreement and Concession Agreement, standard Warranties have been given, and these are set out in Exempt Appendix I (ii).
46. Certain obligations remain with the Council which were negotiated as part of the procurement. These are limited to pension obligations for transferring employees as noted above, and a share of redundancy and pension strain costs if any of the transferring employees are made redundant by the SP within the first three years. This could range from £167k to £213k based on 22/23 pay rates.
47. One indemnity is being provided in respect of land ownership which parts of the heat network cross.
48. The S151 Officer will need to determine the appropriate level of provision against the contingent liabilities outlined above and captured in the CBA in Annex A

Value of Assets transferring to City Leap

49. Under the terms of the Share Purchase Agreement (SPA), the consideration payable will fully recover the non-grant funding cost incurred by the Council in building the networks, up to the point of signing the SPA.
50. Final reconciliations will need to be prepared to ensure all costs are fully captured and included in the final Completion Accounts to be completed in accordance with the terms of the SPA.
51. The estimated value of the assets being transferred are set out below, showing the expected value at month-end through to 31 March 2023, noting that contract close is expected in early January 2023.
52. This forecast has been shared with the Preferred Bidder, and whilst subject to their due diligence, is not expected to alter significantly, though is subject to normal variation for actual costs incurred.

File 8.31

Network	EIF Forecast - 09.11.22 - Gross Cost to 31.03.23							Total
	Actual YTD Sep	Fcst Oct	Fcst Nov	Fcst Dec	Fcst Jan	Fcst Feb	Fcst Mar	
Phase 1 *	6,663,399							6,663,399
Redcliffe Phase 2	8,224,461	225,032	239,794	127,479	121,855	264,143	92,301	9,295,064
Old Market	17,191,742	(38,160)	111,911	358,900	246,112	41,120	77,384	17,989,009
Bedminster	3,526,464	462,514	490,962	350,595	356,057	283,452	440,772	5,910,816
PSDS	6,924,542	151,813	158,637	251,353	264,064	61,430	2,263	7,814,103
Asset Value	42,530,608	801,199	1,001,304	1,088,327	988,088	650,146	612,720	47,672,391
Temple	544,224	17,542	22,884	35,417	58,398	143,269	73,736	895,469
Asset + Deferred Grant	43,074,832	818,741	1,024,188	1,123,743	1,046,486	793,414	686,456	48,567,860

* Net of adjustment NBV

Network	EIF Forecast - 09.11.22 - Net Cost to 31.03.23							Total
	Actual YTD Sep	Fcst Oct	Fcst Nov	Fcst Dec	Fcst Jan	Fcst Feb	Fcst Mar	
Gross Cost	43,074,832	43,893,573	44,917,761	46,041,504	47,087,990	47,881,404	48,567,860	48,567,860
Grant Income	(22,467,071)	(22,467,071)	(22,467,071)	(22,467,071)	(22,467,071)	(22,467,071)	(22,467,071)	(22,467,071)
Phase 1 adj (Incl Above)	(215,552)	(215,552)	(215,552)	(215,552)	(215,552)	(215,552)	(215,552)	(215,552)
Net Cost 31.03.23	20,392,209	21,210,950	22,235,138	23,358,881	24,405,367	25,198,781	25,885,237	25,885,237

53. EY were commissioned to advise on all tax related matters in connection with City Leap and the transfer of assets and have advised that the transfer of these assets would not be subject to VAT, as it would fall under the Transfer of a Going Concern principle (TOGC).

54. Accordingly, no VAT will be applied to the initial transfer, but will apply to any additional costs incurred post 7 December 2022 (see BHNL Cash Flow under para 58).

Protecting for the Council - Determination of Contractual Liabilities & Closing Accounts

55. As part of the transfer to BHNL work is ongoing to agree all contractual commitments, and cost incurred, at the point of novation with the principal suppliers (contractors). The work is nearly complete and, to provide an indication of scale, seven contractors account for 80% of all external third party spend forecast to be circa £4.3m for the period October to March (see summary below).

HNA Forecast x Suplier - October 2022 - March 2023			Fcst	Fcst	Fcst	Fcst	Fcst	Fcst	Total	% Total
ID	Network	Novate / Assign	Oct-22	Nov-22	Dec-22	Jan-23	Feb-23	Mar-23		
Total										
1	3D-Technical Design Limited	Yes	8,434	77,649	44,414	6,500	48,000	32,000	216,996	4.0%
36	CSW Process Ltd	Yes	488,254	499,868	322,123	154,359	383,718	327,783	2,176,105	40.1%
44	F P Hurley & Sons Ltd	Yes	43,991	-	-	-	-	-	43,991	0.8%
52	Goram Homes Limited	Yes	(117,832)	-	-	191,758	-	-	73,926	1.4%
58	Heat Network Associates Limited	Yes	180,571	-	74,031	74,031	42,587	42,587	413,807	7.6%
63	Jewsons Ltd	Yes	-	-	257,734	-	-	-	257,734	4.8%
92	Therma-Mech LTD	Yes	88,134	241,819	305,319	279,509	192,241	51,263	1,158,285	21.4%
Total			691,551	819,336	1,003,622	706,157	666,545	453,633	4,340,845	80.0%

56. It is expected that all liabilities and obligations will pass to BHNL via the novation / assignment of relevant key contracts.

Funding Requirements of BHNL

57. As a risk mitigation in the event the transaction is delayed, BHNL have set out a high-level Cash Flow, based on the forecast noted above, and are seeking an extension to the existing facility of £2m.

58. The analysis shows that this extension will be required to meet a funding requirement of £1.1m in January rising to £1.6m in March over the currently approved facility of £24m, if the deal is delayed for any reason. This would contain the costs in the revised funding envelope for 22-23 and as the issue is expected to be one of timing only, and there is no expectation from the Preferred Bidder that work is put on hold, any increase in funding, arising from delays in the transaction, would be recoverable under the terms of the SPA, subject to due diligence.

File 22.1BP....

BHNL CASH FLOW FORECST to 31 March 2023

£'000	Nov-22	Dec-22	Jan-23	Feb-23	Mar-23	Total
Opening Cash	1,378	(162)	289	(1,141)	(654)	1,378
Revenues, Connection Fees, A/R	1,585	211	236	1,561	378	3,971
VAT	5	-	-	390	-	395
Loan Drawdown *		23,700				23,700
Asset Transfer (less deferred grant) **		(21,211)				(21,211)
SDLT		(500)				(500)
Opex, A/P	(1,743)	(255)	(266)	(381)	(357)	(3,001)
Ongoing Capex + VAT	(1,229)	(1,348)	(1,256)	(952)	(824)	(5,609)
Loan Interest	(159)	(145)	(145)	(131)	(145)	(724)
Closing Cash *	(162)	289	(1,141)	(654)	(1,601)	(1,601)
Loan Facility Utilised / Required	300	23,711	25,141	24,654	25,601	
* Non Cash Drawdown						
** Forecast October		24,000				

Approved Level of Borrowing July 2022 Cabinet

Indicative Capital Investment

59. The Table below sets out an extract from the Illustrative Heat Model (v 3.1) to show the investment that has been made, and which would have to continue to be made, to complete the networks still under construction.

60. For clarity, this does not represent the planned investment by the Council.

61. It should be noted that approval for the Temple Network has not been subject to Cabinet approval, save for the commercialisation phase which is fully grant funded.

EIF Live 221102	2022/23	2023/24	2024/25	2025/26	2026/27	2027/28	Total
Old Market	17,987,775	980,429	-	-	-	-	18,968,204
Redcliffe Phase 2	9,299,087	-	-	-	-	-	9,299,087
PSDS	7,814,332	-	-	-	-	-	7,814,332
Bedminster	5,910,817	190,000	2,759,984	3,100,956	-	-	11,961,757
Temple	896,269	1,915,037	3,177,190	5,791,317	4,735,610	3,818,250	20,333,673
Redcliffe / Temple Phase 1	6,663,399						6,663,399
Total	48,571,679	3,085,466	5,937,174	8,892,273	4,735,610	3,818,250	75,040,452
Excl Temple	47,675,410	1,170,429	2,759,984	3,100,956	-	-	54,706,779

Cost-Benefit Analysis

62. Annex A sets out the Indicative Cost-Benefit Analysis to the Authority of appointing a City Leap Strategic Partner.
63. It shows for the initial five-year period an overall Indicative NPV of just under £1.9m
64. Whilst it is acknowledged that financial returns can be made beyond the initial 5-year period, the overarching objective of City Leap, beyond bringing private sector expertise and funding to the table, is to assist the Council in achieving its net zero targets by 2030.
65. Furthermore, the scale of investment required as set out in the SP's Tender bid submission is not insignificant and by appointing a Strategic Partner, the Authority:
 - a. Frees-up capital for investment in other key Council initiatives
 - b. Removes the need for the Council to deploy and manage large-scale commercial deployment of low carbon infrastructure, and the risks that go with that
 - c. Enables the Council to focus on other social and economic areas of need in the community and just transition
 - d. De-risks the large-scale investment that is required to deliver the City Leap outcomes
 - e. Flexible and agile delivery platform and funding models which can be layered in an integrated placed based manner across multiple asset classes
66. Additional wider economic and social value benefits are also delivered, though outside the scope of this commentary.

P Keegan

Finance Business Partner, City Leap

25 November 2022

Annex A – Cost Benefit Analysis

Indicative Cost-Benefit Analysis of granting the Concession to the City Leap Preferred Bidder - £m							25-Nov-22 PK
5 Year MTFP Indexed		FY 22-23	FY 23-24	FY 24-25	FY 25-26	FY 26-27	Total
Savings / Benefits							
Concession Payment	Guaranteed	1.42	0.07	0.16	0.23	0.18	2.05
Authority Share Payment	Not Guaranteed	0.12	0.22	0.45	0.64	0.65	2.09
Risk adjust Non guaranteed Payments	Delayed Income / Capex	(0.02)	(0.04)	(0.09)	(0.13)	(0.13)	(0.42)
Savings ES Budget	Yr 1 assumes 3 months	0.13	0.51	0.51	0.51	0.51	2.18
Total Incremental Income / Savings		1.64	0.77	1.03	1.26	1.21	5.91
Offset by:							
Mobilisation Costs	To 31 March 2023	-	-	-	-	-	-
Client Function	-	(0.26)	(0.51)	(0.51)	(0.51)	(0.51)	(2.32)
In demnities	Pension Strain costs 50%	(0.05)	-	-	-	-	(0.05)
In demnities	Redundancy 50%	(0.17)	(0.02)	(0.02)	-	-	(0.21)
In demnities		(0.30)	-	-	-	-	(0.30)
Write-Off Phase 1 Assets	-	(0.50)	-	-	-	-	(0.50)
Total Incremental Costs / Lost Income		(1.28)	(0.54)	(0.54)	(0.51)	(0.51)	(3.38)
Net (Cost) / Benefit		0.36	0.23	0.49	0.74	0.70	2.53
NPV @ HM Treasury Real + Inflation @ 5% (Nominal)		0.34	0.20	0.38	0.53	0.46	1.91
Estimated Capital Investment Saving (from January 2023)		2.25	1.17	2.76	3.10	-	9.28
Estimated tCO2 Saving	Per Revised Business Plan Nov'22	17,955	13,798	36,931	42,471	41,736	152,891

END