



Belfast City Council

Report to:	Strategic Policy & Resources Committee
Subject:	Energy – Proposed New Procurement Strategy
Date:	20 September 2013
Reporting Officer:	Gerry Millar, Director of Property & Projects, Ext: 6217 Ronan Cregan, Director of Finance & Resources, Ext: 6184
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1.0	Purpose
1.1	The purpose of this report is to propose a new procurement strategy for gas and electricity to deliver value for money, efficiency savings and support a cost avoidance strategy (minimise future increases in energy costs) on the understanding of accepting a risk-based approach to energy procurement. This proposal is specific to gas and electricity procurement only and does not include oil.
2.0	Background
2.1	The SP&R reports of June and April 2012 identified delivering further energy savings across the Council as a key priority for the 2014-15 and 2015-16 efficiency programmes. In the financial year 2012-13 the Council spent £3.54m on electricity and gas: £1.96m and £1.58m respectively. Our spend on energy has increased by £600k between 2010/11 and 2012/13 which represents a 21% increase. In terms of the domestic energy market this market is unstable and future costs are likely to fluctuate. For information, our top 15 sites for both electricity and gas consumption are listed in Appendix 1 .
2.2	The Council's energy consumption will be affected by any future acquisition and disposal of assets. A reduction in energy consumption can only be achieved through energy efficiency projects and better in-house management of energy consumption, for example the current roof survey of Council buildings to examine their suitability for solar power. This report focuses on managing the price we pay for energy regardless of any changes to our asset portfolio and energy efficiency.
3.0	Outline of approach
3.1	Currently the Council procures energy via a fixed price tender through participation in a Northern Ireland Local Authority regional energy framework. Using this approach the tender prices are wholly dependent on the relatively small supplier margin (around 5%).
3.2	Many large organisations are now using energy management companies to manage their energy costs, specifically their wholesale energy costs. Typically this involves agreeing and setting an energy budget for a 1-5 year period which is managed in a flexible way by the company. This means the company would use hedging techniques (i.e. trades to protect against adverse price movements) to ensure that the price we pay is below the market price. By way of example, Ireland's National Procurement Service uses this approach for 98% of the public estate and saved €21m in 2011-12

	(13% of their annual energy cost).
3.3	The potential for savings using this procurement approach, i.e. by influencing the market price, is much higher than our current procurement approach where any savings would be only on the supplier profit margin.
3.4	The price we pay might fluctuate but should not exceed the expenditure level set by us as part of our budget estimating process. The estimates for 2013/14 have been set and agreed at £3.6m and excluding inflationary increases this price will not be exceeded under this proposed arrangement for 2014/15. The level we set will be monitored and reported by the company appointed on a daily basis as part of the contract. We can also choose to fix a percentage of our portfolio and have a flexible approach to the remainder. If this managed service approach is adopted the majority of the expected efficiency savings will be realised from year 2 onwards. A further benefit is that we will definitively know what the projected level of efficiency savings will be for year 2 and 3 almost immediately after commencing the contract in year one allowing us to set more accurate budget expenditure estimates for the subsequent years.
3.5	Other services usually provided by these companies include an ongoing service to validate energy invoices to ensure the accuracy of our future energy bills and also a historic cost audit where they will review previous bills for any errors.
4.0	Potential efficiency savings
4.1	Based on 2012-13 volumes and prices, the Council could have saved £379k on its total energy bill (£227k on electricity and £153k on gas). These figures are based on using a fully flexible approach and using market prices provided by a supplier in the course of this research. Depending on the fixed/flexible approach taken the savings will vary. Please see Appendix 2 for graphs illustrating the potential savings.
4.2	There are costs associated with this service. Indicative costs provided to the Council in the course of researching this approach are approximately £70k per annum. It would be expected that costs received by suppliers through a tender or framework process would be lower.
4.3	Based on our costs incurred during 2012/13 if we had already been in the managed service arrangement, the potential savings for the first year could have been between £81k and £309k depending on the approach to risk management we adopted involving either a part-flexible managed service or based on a fully flexible managed service.
4.4	As Members will be aware, our efficiency savings are measured by a reduction in our budgets (cash savings). The 2013-14 corporate total for our combined gas, electricity and CHP budget is £3.6m and departments have been advised to allow for an inflationary increase of 5% as indicated in the High Level Rates Guidance Report for 2014-15. The need to adopt a more proactive approach to energy procurement is supported by the recent trend of increasing energy costs which is a trend that is predicted to continue over the coming years. It also highlights the need for us as an organisation to source more innovative procurement mechanisms to maximise the opportunities to reduce our energy expenditure costs going forward.
4.5	It is envisaged that this approach should also lead to in-year savings which could be earmarked to fund or hedge future Council energy costs to further reduce the budgets of future years.
5.0	Outline of options
6.1	The Council currently has two procurement options to consider: Option 1: Continue with current status quo . Option 2: Engage an energy management company to provide a managed service solution to energy procurement.

	<p>Option 2 as it is presented above can take two forms:</p> <ul style="list-style-type: none"> part-flexible/part-fixed approach which allows us to set a fixed cost to a percentage of our portfolio and have a flexible approach to the remainder; or fully flexible portfolio approach.
6.2	The main advantage of using Option 1 is certainty of cost regardless of global and domestic market conditions, while the main advantages of using Option 2 is to benefit from any market fluctuations, both increases and decreases in price. A summary of the associated advantages and disadvantages of each of these options is set out in Appendix 3 .
6.3	A decision on whether to use a part-flexible or fully flexible portfolio management approach does not need to be made until later on in the process when the appointed supplier would advise us by facilitating a risk management workshop with relevant senior officers. The Council can also elect not to proceed with the process at this stage and simply enter a fixed price contract as is the current arrangement.
8.0	Resource Implications
8.1	There will be no additional resource human resource implications required as this process can be managed within existing resources and the new procurement approach if approved would reduce the number of energy-related procurement exercise carried out by the Council. Option 2 if approved can also present more scope to realise efficiency savings and cost avoidance.
9.0	Equality and Good Relations Implications
9.1	None
10.0	Recommendations
10.1	<p>The Committee is asked to:</p> <ul style="list-style-type: none"> Consider the contents of this report and to give approval to explore Option 2 using the managed service approach further in the context of reviewing the scope for realising efficiencies as part of the rate setting process. If approval is given to progress Option 2 Committee is asked to give authority to commence a tender process to appoint an energy management supplier and to delegate authority to the Director of Property and Projects to oversee this process and appointment.
11.0	Documents attached
11.1	Appendix 1 – Top 15 sites based on energy consumption 2012-13
11.2	Appendix 2 - Potential savings based on fixed/flexible approach
11.3	Appendix 3 – Summary of associated costs and benefits of both options

Appendix 1 – Top 15 Sites based on energy consumption 2012-13

Electricity (total annual spend in 2012-13 – £1.96m)

Rank	Main Site Name	Cost Site Total	% of total Electricity costs	% of total Energy costs
1	Waterfront Hall	181,640	9%	5%
2	Belfast Zoo	179,213	9%	5%
3	Belfast City Hall	162,211	8%	5%
4	Duncrue complex	125,166	6%	4%
5	The Cecil Ward Building	105,416	5%	3%
6	Grove Well Being Centre	95,150	5%	3%
7	Adelaide Exchange Building	87,444	4%	2%
8	Information Services Belfast (ISB)	76,692	4%	2%
9	Avoniel Leisure Centre	55,606	3%	2%
10	Ulster Hall	54,669	3%	2%
11	Belfast Castle	52,049	3%	1%
12	Whiterock Leisure Centre	49,076	3%	1%
13	Falls Leisure Centre	46,458	2%	1%
14	Andersonstown Leisure Centre	45,862	2%	1%
15	Shankill Leisure Centre	39,948	2%	1%

Gas (total annual spend in 2012-13 – £1.58m)

Rank	Main Site Name	Cost Site Total	% of total Gas costs	% of total Energy costs
1	Grove Wellbeing Centre	159,293	10%	5%
2	Shankill Leisure Centre	150,018	9%	4%
3	Waterfront Hall	131,794	8%	4%
4	Belfast Zoo	110,201	7%	3%
5	Andersonstown Leisure Centre	95,003	6%	3%
6	Falls Swim Centre	92,575	6%	3%
7	City Hall	89,487	6%	3%
8	Ballysillan Leisure Centre	80,191	5%	2%
9	Roselawn Crematorium	69,166	4%	2%
10	Whiterock Leisure Centre	66,551	4%	2%
11	Avoniel Leisure Centre	64,127	4%	2%
12	Olympia Leisure Centre	61,415	4%	2%
13	Botanic Gardens (Palm House)	50,217	3%	1%
14	Duncrue Depot	45,860	3%	1%
15	Cecil Ward Building	36,763	2%	1%

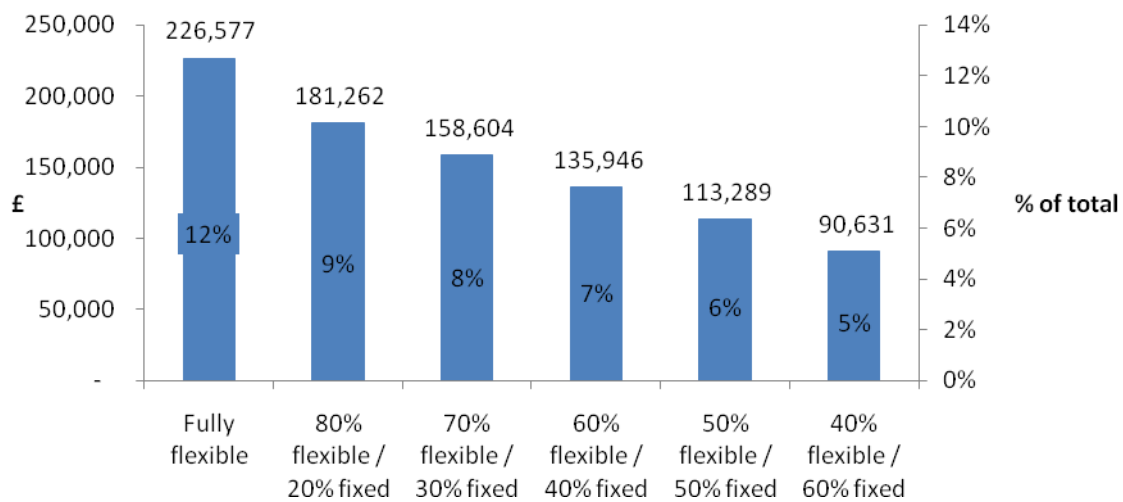
Total Energy (total annual spend in 2012-13 – £3.54m)

Rank	Main Site Name	Cost Site Total	% of total Energy costs
1	Waterfront Hall	313,434	9%
2	Belfast Zoo	289,414	8%
3	Grove Wellbeing Centre	254,443	7%
4	Belfast City Hall	251,698	7%
5	Shankill Leisure Centre	189,965	5%
6	Andersonstown Leisure Centre	140,865	4%
7	Duncrue complex	125,166	4%
8	Avoniel Leisure Centre	119,733	3%
9	Whiterock Leisure Centre	115,627	3%
10	Ballysillan Leisure Centre	110,283	3%
11	The Cecil Ward Building	105,416	3%
12	Olympia Leisure Centre	93,689	3%
13	Falls Swim Centre	92,575	3%
14	Roselawn Crematorium	89,971	3%
15	Adelaide Exchange Building	87,444	2%

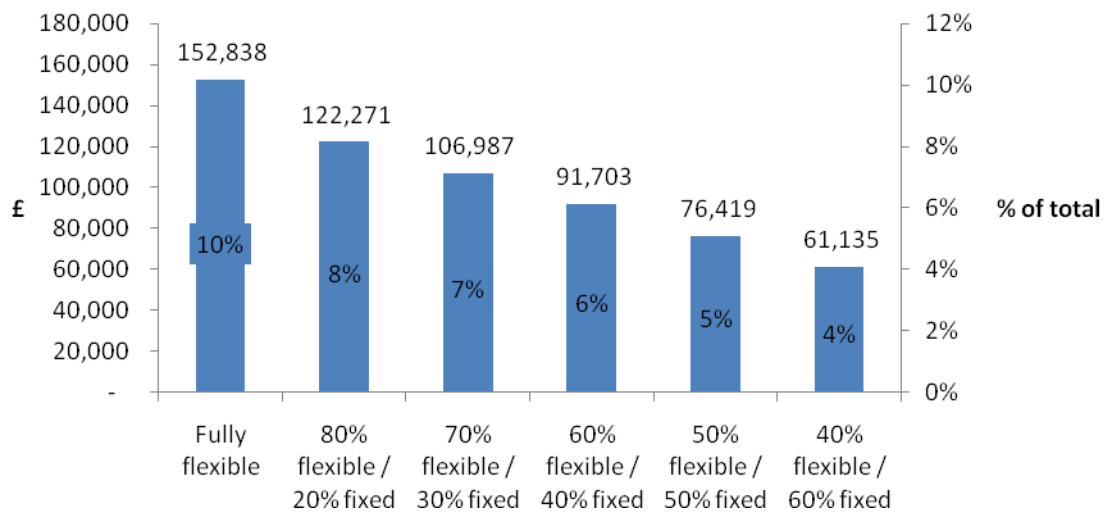
NB Please note that this is based on our 12-13 bills, please use as a rough indication of our energy usage ranking by site.

Appendix 2 – Potential savings based on fixed/flexible approach

Potential savings based on 2012-13 volumes and prices - Electricity only



Potential savings based on 2012-13 volumes and prices - Gas only



Potential savings based on 2012-13 volumes and prices - Total

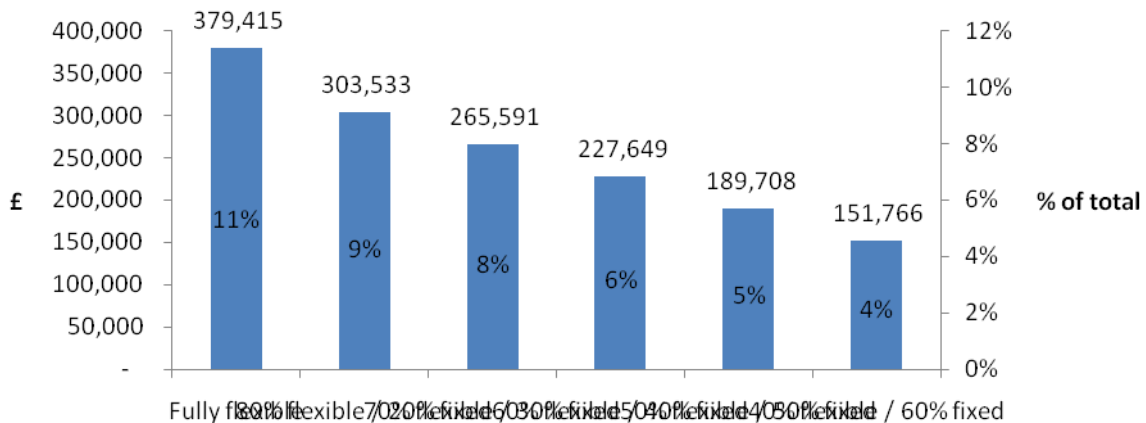


Table on which these graphs are based:

	Electricity		Gas		Total	
	Potential savings (£)	% of Electricity total	Potential savings (£)	% of Gas total	Potential savings (£)	% of total
Fully flexible	226,577	12%	152,838	10%	379,415	11%
80% flexible/ 20% fixed	181,262	9%	122,271	8%	303,533	9%
70% flexible/ 30% fixed	158,604	8%	106,987	7%	265,591	8%
60% flexible/ 40% fixed	135,946	7%	91,703	6%	227,649	6%
50% flexible/ 50% fixed	113,289	6%	76,419	5%	189,708	5%
40% flexible/ 60% fixed	90,631	5%	61,135	4%	151,766	4%

NB These are estimates based on 2012-13 volumes, the prices BCC locked into for contract period versus the market natural gas price provided by a supplier.

Appendix 3 – Summary of associate costs and benefits of both options

Option 1: Continue with current **fixed price** tender approach

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<ul style="list-style-type: none"> • Certainty of price we pay regardless of market prices 	<ul style="list-style-type: none"> • Fixed price only allows relatively small supplier profit margin as potential price differential leading to smaller potential efficiency savings • Unable to take advantage of falling natural gas prices • Fixed price contract does not allow for increase above agreed capacity levels

Option 2: Engage an energy management company to provide a **managed service** solution to energy procurement

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<ul style="list-style-type: none"> • Capture benefits of falling natural gas prices • Can monitor position on a daily basis • Although energy supplier prices are increasing currently future natural gas prices are cheaper than current prices (due to anticipated increased supply in domestic market) • Flexibility on volumes i.e. you can change the size of your assets portfolio and expected volumes without penalty 	<ul style="list-style-type: none"> • Potential exposure to unforeseen events in global market • Upper budgetary limit may be higher than current fixed cost (dependent on fixed prices received)