

<b>Item No.:</b> 13	<b>Classification:</b> Open	<b>Date:</b> 18.07.2006
<b>To</b>	Executive	
<b>Report title</b>	<b><i>Gateway 1: Procurement Strategy Approval for the selection of Private Sector Partners for a Multi Utility Services Company</i></b>	
<b>Ward(s) or groups affected</b>	Chaucer; Walworth; Newington; Faraday	
<b>From</b>	Director of the Elephant and Castle and Special Projects	

## RECOMMENDATION

1. That the Executive approve the procurement strategy outlined in this report for the procurement of Private Sector Partners (PSPs) to form a Multi Utility Services Company (MUSCo).

## BACKGROUND INFORMATION

2. A 'MUSCo.' In the context of this report is a company proposed to be set up to create and operate infrastructure at the Elephant & Castle with particular emphasis on heat and power generation and distribution, area-wide data cabling and the supply of non-drinking water. It may also extend to the mechanical handling of waste products. The general intention is that the company should operate commercially in such a way as to discharge the planning obligations created by the council's adopted planning guidance. At this stage the option of the council itself taking a stockholding in the company (if created) remains open, but no decisions are sought at this point beyond approval to test the level of market interest in the opportunity. As the report sets out, considerable work has already been undertaken to establish how the council's demanding carbon reduction and other environmental targets for the Elephant might be achieved, and work is planned to continue. The early results suggest that a viable business model might be created, hence the proposal to test this in the open market using European procurement arrangements. However, it should be stressed that nothing in this process creates any new obligations. At the point that results are reported back from the market testing exercise, members will be able to judge the general merits of the proposal and assess the specific responses from commercial infrastructure developers and operators.
3. The Supplementary Planning Guidance (SPG), Feb 19 2004, for the Elephant and Castle promotes a significant growth at the Elephant and Castle. A total of 6.5 million square feet of new mixed-use development is proposed. This will almost triple the amount of floor space. In order to mitigate the environmental impacts of substantially increasing the density of development at the Elephant & Castle, the SPG sets ambitious targets for reducing carbon emissions and minimising the use of treated water for non-potable use, aiming to move towards a carbon neutral scheme with significantly reduced energy and potable water consumption, and a significant contribution to carbon abatement from renewable energy technology and fuel. In support of these objectives the Council has secured the backing of the Mayor for London, who recently designated the Elephant and Castle opportunity area as an Energy Action Area (EEA), and the London Climate Change Agency (LCCA), who are providing support on technical aspects of the procurement process.
4. Both the GLA and the LCCA recognise that the regeneration of Elephant and Castle provides a unique opportunity to introduce a mix of sustainable energy and water management infrastructure on a project of significant scale and importance in a London context. Through the adopted Development Framework and subsequent Lead Partner procurement process, the council has proposed best practice targets for energy and water efficiency, the deployment of wind, solar and biomass renewable energy technologies, and the phased roll out of an area-wide sustainable infrastructure network that will connect individual sites to a community heating,

cooling and power system, a supply of non-potable 'green' water and 'fibre to the unit' data services.

5. The GLA's support has been further re-affirmed through the planning and development control process for the recently consented schemes at 50 New Kent Road (the Volvo Garage Site) and Castle House. By working together, LB Southwark and the GLA have secured, through section 106 agreements: firm commitments for the future connection of both developments to the proposed MUSCo; contributions towards a dual plumbing system capable of supplying untreated groundwater for non-potable use; and a contribution towards the proposed trial wind turbine installation on Ashenden House. Critical to this success has been the council's proposal to create a hybrid sustainable energy system that can be re-provisioned with new technology and refuelled with renewable fuels, as and when it becomes commercially viable to do so.

### Low Carbon Energy

6. The strategy for addressing the area-wide energy objectives within the adopted Elephant and Castle SPG is as follows: -
  50. Best practice energy efficiency targets for all new buildings;
  51. The installation of combined heat and power plant (CHP) and recovery of waste heat for cooling;
  52. A minimum 10% contribution from building mounted/ building integrated renewable energy technology and locally derived sources of renewable fuel by the time the development is completed;
  53. Establish a special purpose Energy Services Company (ESCO)
7. To date, work has been carried out to establish a more detailed energy profile of the development proposals, based on current good practice and recommended best practice energy efficiency standards. This has informed the strategic modelling of energy and emissions to determine the balance of energy efficiency targets, CHP and renewables required to achieve zero carbon growth.
8. The council's technical team have undertaken an energy centre planning study and are now at a relatively advanced stage with a commercial proposition for an area-wide distributed energy infrastructure. Proposals include two new energy centres providing in the region of 5 to 6 MWe of CHP capacity: the first of these to be located at St Mary's churchyard and the second to be sited at Heygate Boiler House. The option to site additional plant below ground adjacent to the Volvo garage site at 50 New Kent Road is also being examined.
9. Detailed numerical modelling of seasonal daily demand patterns for heat and power has now been completed and these have been used to determine the proportion of on-site demand which could be supplied from local generation, the back-up and top-up required from boiler plant and the local power distribution network, and the potential revenue streams, annual operating and maintenance costs associated with the roll out of community heating and power on an area-wide basis.
10. A schematic design for a typical energy centre has been prepared in order to assess the likely land-take and building massing implications of locating energy plant within the core development area. The energy centre at St Mary's Churchyard would also create an opportunity for a data management and environmental resource centre facing onto the rejuvenated park.

### Non-potable 'green' water supply

11. Non-potable ('green') water provision is a planning requirement for the whole of the Elephant and Castle redevelopment. The proposed 'green' water supply system is to be based on the installation of two groundwater abstraction wells located at opposite ends of the core development area, at Stead Street and St Mary's Churchyard. These will draw water on a sustainable basis from the underlying chalk aquifer to provide 100% of the non-potable demand of the Elephant and Castle redevelopment (approximately 30 to 40% of the total annual water demand). Non-potable uses are envisaged to include: construction; toilet flushing; hand basins (commercial buildings only); public area cleansing; landscape establishment and street cleaning. It is estimated that the council could save as much as £10,500 per year in water bills if the borehole system is licensed on an area wide basis. To date, Environment Agency consent to drill and test has been granted and tender documents have been prepared for issue to drilling contractors. The borehole location at Stead Street has been incorporated into the Development Brief for early housing on the site.

### Data services

12. It is proposed that 'fibre to the unit' infrastructure be co-located with the low carbon energy and 'green' water infrastructure, and simultaneously delivered by the MUSCo. The proposed infrastructure will create a true broadband capable local loop (intended to be accessible to a range of service providers). The intention is to facilitate the delivery of next generation connectivity helping to attract and retain businesses, providing an asset for local people and enhancing the social inclusion activities of the Council. The system is intended to also provide a means for the Southwark Council and other service providers to deliver their services more efficiently. In particular, the delivery of e-government, e-inclusion and enhanced information giving. It is also envisaged that a fibre to the unit infrastructure will provide a platform for billing activities associated with the delivery of MUSCo services, and assist in the delivery of intelligent buildings within the development by enhancing the energy efficiency of buildings in operation and reducing energy consumption.

### Statutory Consultees and Utilities

13. The conventional infrastructure needed to support the sustainable redevelopment of the Elephant and Castle is also being looked at thoroughly and Southwark Council are in consultation with National Grid Transco, Thames Water Utilities and EDF Energy to assess the level of reinforcement to existing primary infrastructure required over time to enable the development to realise its full capacity. The council are also holding regular external meetings with the Environment Agency to ensure that its proposals for a groundwater supply are aligned with the recently published Catchment Abstraction Management Strategy for London, and have consulted internally to make sure that the recording and monitoring of water quality is properly addressed from an environmental protection standpoint. We have also apprised Environmental Protection of the proposals to construct new energy centres at the Elephant and Castle.

### Multi-utility Services Company (MUSCo)

14. To advance the MUSCo proposals the development team have been working closely with its technical and legal team on the various business models, infrastructure, regulatory and legal issues surrounding the establishment of a MUSCo. In addition, Donaldson's LLP are in the process of developing an outline business and financial model as a base-case for negotiation with short-listed private sector partners (PSPs). The CAPEX, OPEX and revenue streams in the model are based on detailed energy profiling and operational modelling of CHP embedded within the current framework for development, the area-wide demand for an untreated supply of non-potable water, uptake of data services based on business and residential occupation of the development area and a wholesale approach to bandwidth leasing. The model will be used to determine key economic drivers, rigorously test the business case for a MUSCo, and carry out a

risk assessment of the underlying operational and financial parameters. It will also have the flexibility required to investigate the economic impact of changes or delays in the phased development of the overall Elephant and Castle Development.

15. A more detailed financial and business model will be developed once the council has decided on its preferred mode of engagement and there is greater clarity about the options for financing the scheme. Clearly in order for the council to derive the greatest benefit from a competitive negotiated procedure it is essential that PSPs are allowed the flexibility to respond to the base case and prepare their own financial proposals which can then be brought forward and developed through a process of dialogue and negotiation. This can only be achieved by launching this procurement process. The full support and cooperation of FMS together with expert advice from external financial consultants will be crucial to a successful outcome at this stage.

### The wider area

16. The Aylesbury Estate lies to the east of the Walworth Road and north of Burgess Park, approximately 0.5km south of the Elephant and Castle. The estate encompasses 285,000 square metres and is home to over 7,500 people. On September 27, 2005 the council's executive committee made the decision to demolish the estate in stages and replace it with 2,200 homes for rent and under housing association control and around 2,700 homes for sale or shared ownership. This decision was supported by 70 per cent of residents who responded to an extensive consultation programme, and the tenants and residents associations. Consultation for the bid to upgrade the district heating system in the Aylesbury Estate revealed resident support for community heating, despite the frequent breakdowns on the estate. We envisage that the redevelopment of the Aylesbury Estate could represent an early opportunity for the extension of MUSCo services; indeed this echoes the desire to develop a grid delivering sustainable energy expressed in the objectives of the North Southwark Energy Action Area.
17. It is clear from the preliminary techno-economic studies and market testing carried out to date that the pattern of energy consumption and potential revenue from sales of electricity and heat associated with a mixed-use development such as that at the Elephant and Castle is a determining factor in making the scheme commercially attractive to the private sector. As currently proposed, The Aylesbury Estate redevelopment is unlikely to benefit from a similar mix of residential and commercial uses. It is proposed therefore that the technical services carried out in support of the masterplanning of the Aylesbury include an urban energy planning task to enable early strategic assessment and decision making around the provision of an integrated energy, water and data services provision across the two developments.
18. The council are cooperating with LUL and London South Bank University to investigate potential synergies between the MUSCo, proposals to install community heating at LSBU's Southwark campus and opportunities for introducing cooling, produced as a by-product of CHP via absorption chilling, at key points in the London Underground network.

### **Context for this procurement**

19. Work performed from the very beginning of the Elephant and Castle Development Commercial Partner selection process has consistently demonstrated that the establishment of a special purpose vehicle to provide an intelligent and coordinated (holistic) approach to the provision of low carbon heat and power, non-potable water and data services infrastructure is essential if the council is to achieve the ambitious targets expressed in the adopted SPG. It has become increasingly evident that the sustainability targets the council has set for the redevelopment of Elephant and Castle will not be achieved by traditional site specific delivery of conventional utility services coupled with a plot by plot, piecemeal approach to development based on 'low carbon' building technology. In particular, work carried out in support of Stage 2 of the Lead Partner procurement process for the Elephant and Castle sets out the council's intention to

establish a special purpose joint venture delivery vehicle (referred to in this document as the MUSCo) as a means of securing the key environmental infrastructure and services required to underpin a sustainable community at the Elephant and Castle.

20. The original assumption for the procurement of private sector partners (PSPs) and delivery of the MUSCo was that the Elephant and Castle Development Commercial Partner procurement exercise would bring partners forward, and obligations would be put on the lead commercial partner to deliver the MUSCo with these partners.
21. However, given the central importance of the MUSCo to the delivery of the council's environmental and social objectives, the emerging timescales and complexities associated with the procurement of the Elephant and Castle Development Commercial Partner and the desire to secure the connection of the early housing sites and other early private sector developments to the network it has become necessary to decouple the procurement of the MUSCo from the Commercial partner selection process. The nature of the MUSCo to be formed as part of this process will be the same as originally envisaged; the Borough will however now play a central role in the identification and procurement of technology and business partners for the MUSCo.
22. Advice from Herbert Smith LLP concluded that a separate but parallel process to the PSP selection process is the most reliable means of ensuring that the demanding targets of the 2004 SPG can be fully met and therefore full planning compliance achieved. It is intended that the two procurement processes will be run in parallel, at all times being mindful of the interface between the two emerging legal frameworks. Accordingly, specialist legal advice will be retained to advise on all aspects of procurement including those issues which require the joint cooperation of the MUSCo and the Lead Development Partner, such as ensuring that all new buildings are connected to the energy, 'green' water and data services network.
23. The Executive has approved the terms of issue of the stage 3 invitation to the remaining shortlist of 3 commercial developers. This decision took full account of the decision to form a MUSCo through a separate procurement exercise and the three bidders are apprised of this fact and by the date of consideration of this report should be in possession of full details as one of the appendices to the final invitation.
24. It is essential that this procurement exercise be concluded in good time to capture all early development in the Elephant and Castle area in order to achieve net zero carbon growth for the Elephant and Castle Redevelopment. In order to achieve this partners must be on board to interface with the Early Housing Sites and the beginning of negotiations with the lead development partner for the Elephant and Castle.
25. Permission for major early developments in the Elephant and Castle: Castle House and 50 New Kent Road has been conditional on the provision of an agreed interface specification designed to appraise developers and their technical teams of the physical measures required to enable a building for future connection to the MUSCo infrastructure. The GLA have allowed Southwark to approve these applications on the basis that a body such as the proposed MUSCo will deliver sustainable energy and contribute towards the renewables target that the GLA have for new development in London.
26. It is clear that a holistic approach to development is the only way to achieve significant mitigation of carbon emissions and minimise reliance on drinking water. This includes the exercise of planning powers, and early planning and delivery of key infrastructure (coordinating with early core development, the delivery of early housing sites and highways infrastructure works.)

### **Overview of the market for the procurement**

27. Significant market awareness raising for this project has taken place over the last year. There is a clear indication that there are a number of willing partners keen to invest in the MUSCo and

be party to its delivery. In addition, from our consultation with the suppliers of consumer items and other technologies it is clear that the provision of true broadband services is key to their long-term business development; they are therefore willing to invest in the development of these networks.

28. As a result of the decision to proceed towards the formal commencement of a MUSCo procurement exercise a Prior Information Notice was published in May 2006. Early indications are that there is strong market interest in both the delivery of technical services and mechanisms of financing the creation of the MUSCo, hence the recommendation to proceed with a full procurement exercise.
29. The formation of joint venture vehicles for the delivery of services is mainstream in continental Europe and is becoming increasingly common in this country: Woking has been a partner in an ESCo delivering CHP for a number of years and GLA has recently formed the London ESCo partnering with EDF energy and BT to deliver connectivity and CHP to the Olympic and Thames Gateway developments. The scale and range of services proposed for inclusion in the MUSCo will make an exemplar project for sustainable development.

### **Summary of the business case**

30. The provision of the CHP and non potable water services backed up with and managed using a true bandwidth ICT infrastructure will enable the London Borough of Southwark to achieve a number of environmental, social and business transformation goals. Surpluses generated particularly by the ownership of the ICT infrastructure will support council revenue streams.
31. Having consulted widely, it is considered that a traditional core utility provision cannot be relied upon to deliver the necessary environmental infrastructure capable of meeting the councils environmental and social objectives within the timescale required for the integration of the core development and surrounding opportunity sites and the planned early housing sites. It is therefore necessary to enter into a form of joint venture (the exact legal form of which may be decided subsequently when its precise role is crystallised) capable of channelling both public and private funds into the timely provision (or management of the provision) of multi-utility environmental infrastructure and services
32. Early financial modelling indicates that capital investment will be paid back and generate surpluses. The business case for Southwark, however is not simply a matter of finances: the ability to deliver net zero carbon growth in a major urban development, ability to attract, retain, and develop new business, which has been a key feature of the delivery of the enhanced communications infrastructure in European cities such as Stockholm and Almere, and community safety gains from the delivery of MUSCo services represent an exercise of Southwark's Well Being Powers detailed in the amended Local Government Act.

## **KEY ISSUES FOR CONSIDERATION**

### **Policy implications**

33. The delivery of the MUSCo is aimed at ensuring that the Elephant and Castle development strives to exceed local and national energy targets.
34. The MUSCo is aimed at enabling developments to comply with sustainability obligations placed on developers by Supplementary Planning Guidance.
35. The Supplementary Planning Guidance for the Elephant and Castle, adopted by Council in 2004, sets out the intention to form an special purpose ESCo (now referred to as MUSCo as water and data infrastructure are included) for the development.

36. In its document "Southwark 2016", the Southwark Alliance lays out an overall strategy for the improvement of Southwark, which includes, among other things, stratagems to enhance service delivery, improve life chances, develop enterprise, enhance community safety, and encourage sustainability. The provision of the MUSCo's infrastructure should raise local ICT infrastructure to enable enhanced public services, encourage and retain businesses, provide an infrastructure for enhanced CCTV and other monitoring technology and provide heat and power services that will enhance the sustainability of all buildings using it.

### High level procurement project plan

Activity	Planned date
<b>Gateway 1:</b> Procurement strategy for approval report (this report)	18/07/2006
Publish OJEU Notice (electronically with PQQ and background documentation)	31/07/2006
Closing date for return of PQQ	05/09/2006
Invitations to Negotiate	26/09/2006
Receive Responses to ITN	12/12/2006
Invite Best and Final Offers	15/01/2007
Receive Best and Final Offers	26/02/2007
Completion of negotiations and partner selection	01/05/2007
<b>Gateway 2:</b> Contract award for approval report	25/05/2007
Contract award	22/06/2007
Monitoring plan implemented	22/06/2007
Communication of new contract to Council	06/07/2007
Contract starts	18/07/2007

### High Level Delivery/Business Plan

37. It is currently envisaged that the MUSCo will bring together LBS, the Elephant and Castle Development Commercial Partner and one or more specialist utility service providers for CHP, non-potable water and data (PSP). The MUSCo will deliver energy, non potable water, heat and data infrastructure for the Elephant and castle development that is capable of being extended to other local regeneration schemes (such as that at the Aylesbury Estate and the Early Housing sites for the Elephant and Castle development) as appropriate. The MUSCo will manage the use of the infrastructure in the case of heat and power as the sole provider, in the case of data as an infrastructure manager offering access to a range of potential service providers which could include (telephony, TV, Internet connectivity) and other procurers of bandwidth available in the network (e.g. Southwark Council, the local primary care trust, local educational establishments, building management companies).

### 38. Intended role of Southwark Council

- Southwark Council will grant leases, licences, wayleaves or other related interests in property as appropriate to the MUSCo for Office, CHP engines and other plant, pipes, cabling and associated infrastructure while retaining its status as the freeholder for this land.
- Southwark Council will select PSPs for the MUSCo.
- Southwark Council could possibly invest in works and infrastructure. The negotiation process will clarify at what stage this will happen. This is particularly appropriate to the development of the combined infrastructure services corridor that will run along Heygate Street and integrate with the spaces left by the then decommissioned subway infrastructure below the land currently occupied by the Elephant and Castle roundabout. The development of this corridor early on, prior to the demolition of the Heygate estate, will give the MUSCo an early opportunity for deployment of services to early sites, which may include a temporary supply of heat to the Salisbury Estate during demolition of the Heygate Boiler House, provide routes for the extension of services and provide an easily serviceable infrastructure corridor for the MUSCo's infrastructure.
- Receives share of surpluses based upon its interest in the MUSCo.
- Assisting in the coordination and creation of productive relationships between the MUSCo and other projects that could deliver power and heat generation or the deployment of data services. Examples of this are the potential development of a waste powered energy generation facility on the Old Kent Road waste processing site, and the proposed upgrade of the council's own ICT infrastructure.
- In the case of the Old Kent Road, while the distances involved and differing timescales of the Elephant and Castle project and the potential project at the Old Kent Road render the idea of locating primary plant for the Elephant and Castle Scheme unviable, Southwark Council will consider the scope for the MUSCo to manage the facility on this site or have some other formal relationship with this proposed facility.
- In the case of Southwark Council's upgrade of its communications infrastructure, account will need to be taken by Southwark Council of the proposed deployment of the MUSCo's services in the North of the Borough. Additionally, Southwark Council will need to facilitate coordination between the MUSCo and Southwark Council's incumbents, both in terms of the integration of infrastructure and enabling Southwark Council's delivery of services to its citizens.

### **39. Intended role of LBS within the MUSCo**

- Joint finance for the deployment of infrastructure during the phased construction of E&C
- Leasing land within the core development area for Energy Centres, ICT exchanges, water treatment, storage and pumping facilities
- Commitment to ensuring that all new buildings within the core development area, regardless of land ownership, are connected to the energy, 'green' water and data services infrastructure

### **40. Intended role of MUSCo Data, Water and Energy PSPs**

In their role as holders of legal interests in the MUSCo the commercial participants will, through various legal and contractual arrangements (either directly or indirectly):

- Take on assets and associated risk from LBS;
- Be involved in joint finance for the design and deployment of MUSCo plant and infrastructure;
- Prepare interface documents as required, giving guidance on mechanical, electrical and public health (MEP) requirements for connection to the site wide energy, 'green' water and data infrastructure, and any temporary connections/ installation of localised plant, or arrangements for future changeover from conventional utility sourced services to MUSCo services;
- Deploy plant and infrastructure (CHP plant, community heating pipework, private wire power network, fibre, heat exchange substations, borehole headworks, water treatment, storage and pumping facilities);
- Manage billing, collect revenues;
- Provide revenue for operational and maintenance costs of plant and equipment

#### **41. Intended role of the Elephant and Castle Development Commercial Partner**

- Enter into a contractual arrangement with the MUSCo Partner
- Possibly take on the role of a funding partner with a legal interest in the MUSCo and in that capacity fund the development of the MUSCo's infrastructure and the continued operation of its activities
- Be obliged through LBS leases to connect individual plots to the MUSCo service infrastructure and possibly to ensure that holders of interests in commercial or residential units take their services from the MUSCo and not from other service providers (subject to relevant industry regulations).
- If required make space in plots available for MUSCo use
- Coordination of civil works
- Place necessary equipment in individual buildings
- Funding for core infrastructure (gas, water supply, drainage, etc) including contributions to the private wire power network and 'green' water supply infrastructure (on a cost neutral basis)
- Joint development of sustainable masterplan proposals accommodating LBS/ MUSCo proposals for the deployment of energy, water and data services plant and infrastructure

#### **Identified risks and how they will be managed**

42. *The Market may not be able to currently deliver partners willing or capable of delivering the services that we envisage.*

An extensive process of market awareness and market testing has been carried out among energy, water, ICT infrastructure suppliers and financial backers. There is increasing interest in this market from mainstream utilities providers who are increasingly expanding their portfolios to consider renewable technologies, district scale provision and the development of localised joint ventures. The financing industry is similarly appraised of the new areas of opportunity that

ventures such as this have made available, and early approaches from organisations who are willing to develop innovative ways of financing the development of the MUSCo have been encouraging. It is clear that there is an appetite for the provision of services within a development such as the Elephant and Castle particularly with the early opportunity of market expansion to the Aylesbury Estate.

43. *Other operators will be able to build infrastructure on the land (without prior consent on streets and without the property owner's consent by obtaining a court order.) Ofcom will encourage sharing of any ducts. This means there is no guarantee for the MUSCO or the commercial partners that it will be the only provider of data infrastructure in the area. In addition, there are restrictions on requiring occupiers/lessees of buildings from taking data services from providers selected by a person with an interest in the building. Where this occurs, the occupier is, notwithstanding any restriction, entitled to choose another provider with the consent of the landlord, which cannot be unreasonably withheld. There is a risk that this might make the commercial proposition unattractive.*

The provision of a local loop capable of delivering true broadband services will provide infrastructure that is open to a range of operators. Other operators would have to finance the capital works required for the delivery of other networks via the provision of additional physical networks; there is a commercial incentive for providers to use the open network that will be provided by the MUSCo. Other operators will not finance the provision of a true broadband capable local loop, as these must be open to other operators. Potential business models and returns for the ICT infrastructure are not predicated on the existence of a local monopoly.

#### **Impact on Lead Partner Negotiations**

44.

45. As indicated previously in this document, the short-listed bidders for the role of lead partner in the Elephant and Castle development have been informed of the MUSCo approach and have not indicated that this route will be problematic.

#### **TUPE implications**

46. N/A

#### **Plans for developing the tender documentation**

47. Tender documentation will be developed by the Elephant and Castle development team in conjunction with its consultant team.

#### **Plans for advertising the contract**

48. The procurement will be advertised in the OJEU

#### **How the responses will be evaluated**

49. The most economically advantageous tender will be selected. Partners will be selected on the basis of a voluntary Competitive Negotiated procedure. This procedure gives Southwark Council the greatest scope and flexibility for specification and development of the MUSCo's structure and financial model.

#### **Effect of proposed changes on those affected**

50. The delivery of an integrated services infrastructure at the Elephant and Castle will enhance the provision of services to its residents, businesses and other stakeholders.

#### **Sustainability considerations**

51. The development of the Multi Utilities Service Company and the exercise of the commensurate controls on energy usage that will be a corollary of this will lead to a physical development at the Elephant and Castle that will be at the forefront of sustainability both in terms of the impact these services will have on carbon emissions, water consumption and the development of a sustainable community of residents and businesses attracted and retained by the efficiencies that the enhanced infrastructure that it will deliver.

#### **Other implications or issues**

52. None

#### **Resource implications**

53. The management of the procurement process to select MUSCO PSPs will require continued input from the Elephant and Castle Development core team and consultant support. These costs which are estimated to be in the region of £150k and can be met from the agreed budget for 2006/7.

#### **54. Financial implications**

The scope of the council's financial commitment is difficult to pinpoint at present. The majority of financing will be sought through private finance, through land deals within the development, and from private sector partners (PSPs). Additional funds from the public sector (EU funds) will be bid for to support the design and deployment of the services network; municipalities in Europe have successfully accessed such funds, we will aim to replicate their success. As the negotiation and bidding process continues in concert with the procurement and business modelling process, the scope to which Southwark will need to invest will be established. During the procurement process, highlight reports will be produced detailing proposed backing from Southwark, and as part of the Gateway 2 report a range of detailed business and financial models will be produced, with input from FMS detailing funding options for the MUSCo. At this time we will also be in a better position to detail the likely return on investment, and therefore the magnitude of surpluses generated by the MUSCo for reinvestment by LBS.

#### **Consultation**

55. The Proposal to form a MUSCo, or as it has been described in earlier documentation EESCo (Energy and Environmental Services Company) has been a key component of the plans for the Elephant and Castle redevelopment since the project was re-launched in 2003 and was one of the key planks of the sustainability strategy adopted as part of the Supplementary Planning Guidance for the Elephant and Castle in 2004. The Elephant and Castle redevelopment has been subject to an extensive process of consultation over the last 3 years, local residents and businesses have been consulted on the panoply of issues related to the development in a series of focus groups, public meetings and statistically robust polling.

56. The ZEN project, a project in which Southwark is also a partner has assessed the view of environmental issues and renewable technologies by residents of the Heygate and Aylesbury Estates. The result of this exercise has been to show clear support for Combined Heat and Power, District Heating and Renewable Technologies.

#### **SUPPLEMENTARY ADVICE FROM OTHER OFFICERS**

##### **Borough Solicitor**

57. The procurement strategy set out in this document takes into account advice received from Herbert Smith on 31 January 2006 regarding compliance with EU procurement law. In essence, the main points of that advice were as follows:

58. The selection of a private sector partner (PSP) by the Council would usually be subject to the EU procurement rules, as implemented by the Public Contracts Regulations 2006;
59. Although the point is not beyond doubt; there is a prima facie good argument that the arrangement with the MUSCo PSP constitutes a public services concession, on the basis that the PSP will bear a substantive part of the economic risk entailed in providing its services. That sharing of risk would be evidenced by the PSP/MUSCo receiving some or all of its consideration or remuneration by charging end-users rather than by the PSP receiving guaranteed fees from the Council. A service concession falls outside the scope of the Regulations but, according to European Court case law, still has to be subject to “a degree of advertising” and competition in order to satisfy EC Treaty principles of transparency and non-discrimination. The Treaty principles do not necessarily require publication of an OJEU notice but such publication would certainly be sufficient to meet those Treaty obligations. Further, following these procedures will provide a robust and tested framework for the procurement process.
60. Herbert Smith therefore recommends that the Council “voluntarily” follow all the steps required under the most flexible procedure under the Regulations, i.e. the competitive negotiated procedure, for two main reasons: first, because of the lack of certainty about the appointment’s categorisation as a service concession and, second, in order to be sure that the Council is complying with its more general obligations under the EC Treaty.
61. Even the recommended course of a competitive negotiated procedure is not entirely free from risk. Recent OGC guidance states that, when awarding complex contracts within the Regulations, public bodies should generally use the new competitive dialogue procedure instead of the negotiated procedure. However, given that there is a good (albeit not certain) argument that the PSP appointment constitutes a service concession, outside the Regulations, Herbert Smith advise that the risk of any objection arising in respect of the use of the negotiated procedure is likely to be low. Moreover, the Council’s strong preference is to use the negotiated procedure because it is more flexible than the competitive dialogue or the other procedures under the Regulations.
62. In a worst-case scenario, a third party supplier could complain that the authority has breached its procurement law obligations, by launching an action in the English High Court and/or by complaining to the European Commission. However, we and Herbert Smith believe that the suggested course (“voluntary” use of a compliant competitive negotiated procedure) strikes the best balance between minimising that risk of challenge, while also ensuring maximum flexibility in the running of the selection process.

## **Head of Procurement**

63. The objective of this procurement is to select a private sector partner to deliver sustainable energy and water services, along with ‘future proof’ data services, within the Elephant and Castle regeneration. This requirement for a ‘MUSCo’ was originally built in to the procurement process for the lead commercial partner.
64. A robust process of market research was undertaken with potential MUSCo providers. In the UK, this is very much an emerging market, which is inhibited largely by the existing regulatory framework governing energy supply. However, it is also clear from the market research that there is strong interest in investing in the Elephant & Castle, provided the Council is prepared to play an active enabling role. This may be simply through land sale and planning agreements, which oblige individual site developers to connect to the MUSCo services. But the report also highlights that there may be a need for the Council to invest in the infrastructure necessary for the MUSCo to operate.

65. Development of the MUSCo procurement approach has taken into account possible links with other projects that are considering similar energy services solutions (e.g. Aylesbury Estate, Canada Water etc.) These links should continue to be explored in the following stages where additional value can be delivered for these projects, without prejudicing the timely delivery of the objectives for the Elephant & Castle.

### Director of Finance

66. Subject to the agreement of the Executive, the Director of the Elephant Links Project Team is committed to carrying out further analysis of arrangements that may be set up to support the creation of a Multi Utility Service Company (MUSCO) and how it may be governed. There is knowledge of similar undertakings already being in place in Europe and there are some smaller schemes operating in the United Kingdom. However, the MUSCO based on the Elephant and Castle site would probably become a ground-breaking scheme by virtue of the size and complexity.

Within an undertaking of this size, it is inevitable that there will be a range of service based and financial risks that the project team will wish to identify. They will also wish to provide containment measures to address each risk. Any financial risks will need to be communicated through the business planning processes already in place for the Council and budget and accounting requirements identified as appropriate for agreement by the Executive and by Council Assembly.

To date, a detailed financial appraisal of this proposal has not been completed although the Director of Regeneration is arranging for the procurement of technical advice and support. This will include specialist advice to review business and financial Modeling. Prior to any decision being taken on the adoption of a MUSCO model, it is critical that the business case is completed and properly verified.

The Finance Director has requested that he be involved in the appointment of appropriate external advisors and will expect to validate their findings.

Subject to the a successful outcome to the project, the Council would wish to seek recovery of all preparatory costs and investments from the partner, developer or other agency benefitting from the longer term arrangement."

### BACKGROUND PAPERS

Background Papers	Held At	Contact
Stage 2 Submissions	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Jon Abbott, 0207 525 4902
Elephant and Castle SPG	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Jon Abbott, 0207 525 4902
Framework for Development	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Jon Abbott, 0207 525 4902

Advice regarding regulatory framework	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Tony Moseley, 0207 525 4903
Advice regarding procurement strategy	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Tony Moseley, 0207 525 4903
Technical Appraisal of Power and Heat Demands in the Framework for Development	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Tony Moseley, 0207 525 4903
Outline Financial Appraisals	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Tony Moseley, 0207 525 4903
ZEN Project "Preferences of the Community" Report	Elephant and Castle Team Third Floor, Coburg House 63-67 Newington Causeway Elephant and Castle London, SE1 6BD	Tony Moseley, 0207 525 4903

## AUDIT TRAIL

<b>Lead Officer</b>	Chris Horn, Director, Elephant and Castle and Special Projects	
<b>Report Author</b>	Tony Moseley, Senior Project Manager, Elephant Links Project Team	
<b>Version</b>	Final	
<b>Dated</b>	July 18 2006	
<b>Key Decision?</b>	Yes	<b>If yes, date appeared on forward plan</b> May 2006
<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / EXECUTIVE MEMBER</b>		
<b>Officer Title</b>	<b>Comments Sought</b>	<b>Comments included</b>
Legal: Borough Solicitor & Secretary	Yes	Yes
Chief Finance Officer	Yes	Yes
Head of Procurement	Yes	Yes
Executive Member	Yes	No
<b>Date final report sent to Constitutional Support Services</b>		