

<b>Item No.</b> 16.	<b>Classification:</b> Open	<b>Date:</b> 25 January 2011	<b>Meeting Name:</b> Cabinet
<b>Report title:</b>		Multi Utilities Services Company (MUSCo) Commercial Partner	
<b>Ward(s) or groups affected:</b>		Cathedral, Chaucer, East Walworth, Faraday and Newington	
<b>Cabinet Member:</b>		Councillor Fiona Colley, Regeneration and Corporate Strategy	

### **FOREWORD – COUNCILLOR FIONA COLLEY, CABINET MEMBER FOR REGENERATION AND CORPORATE STRATEGY**

1. It is with disappointment I recommend that work should cease on the Multi-Utility Services Company (MUSCo) project.
2. It is regrettable that we are unable to conclude this project with our preferred bidder, but we had to be absolutely certain that their proposal presented best value for the council, was a workable model with which to proceed, and that it presented no material risks to the regeneration projects going ahead. We were not satisfied that this was the case.
3. However, the council remains a committed champion of sustainable development and I remain confident that the schemes which we will put in place for the Elephant and Castle, and the Aylesbury, and those existing elsewhere across our housing stock, incorporate really robust measures to achieve the same results.
4. We retain our zero carbon growth strategy for the Elephant and Castle development and, in accordance with the London Plan, a major part of this must be through the use of renewable sources of energy and low-carbon technology.
5. Elsewhere the council continues with other major carbon reduction schemes such as the proposed SELCHP scheme, the only 'waste into power' facility of its kind in London, which aims to capture the heat currently wasted at the plant to heat up to five nearby estates. The Peckham Low Carbon Zone, which is one of only 10 in London, has an overall target of reducing CO<sub>2</sub> emissions across homes, schools and businesses by 20.12% by 2012.
6. While the termination of the MUSCo process is disappointing I remain confident we can meet our targets through alternative means.

### **RECOMMENDATIONS**

7. Cabinet note the progress made to finalise the Dalkia consortium's Best and Final Offer (BAFO) for a Multi Utilities Services Company (MUSCo) Commercial Partner since the Major Projects Board meeting of 19 June 2008.
8. Cabinet note the contents of the BAFO as described in paragraphs 42 – 55.
9. Cabinet note the conclusions of the evaluation of the BAFO and instructs officers to terminate the Dalkia consortium's position as preferred bidder.

10. Cabinet instructs officers to cease work progressing the procurement of a MUSCo solution and that the Deputy Chief Executive is asked to seek alternative solutions to providing services and reducing carbon for the Elephant and Castle and Aylesbury regeneration projects.
11. Cabinet instruct the Strategic Director of Environment and Housing to look into the feasibility of decentralised energy networks to reduce carbon emissions for Council social housing.

## **REPORT SUMMARY**

12. This report seeks the Cabinet's approval to a number of recommendations in relation to the MUSCo project, including the termination of the Dalkia consortium as preferred bidder.
13. The report describes the background to the development of the MUSCo and the procurement process undertaken leading to the appointment of the Dalkia consortium as preferred commercial partner.
14. Whilst the Dalkia consortium's technical proposal has merit, for the reasons detailed in the closed report, officers are unable to recommend acceptance of the Dalkia consortium's Best and Final Offer.
15. Overall the proposals represent a high degree of uncertainty and potential risk to the Council. There is insufficient evidence, details of which are set out in the closed report, for officers to be in a position to conclude that the proposed arrangements represent value for money. Officers are not persuaded that allocating further time and cost to resolving outstanding issues would result in a satisfactory outcome within a timeframe required to complete the process without impacting negatively on the wider regeneration schemes.

## **BACKGROUND INFORMATION**

### **Introduction**

16. At the time the Dalkia consortium was selected as the preferred bidder for the MUSCo it was recognised that considerable work remained to be done to get to the position where the parties could sign the documentation necessary to record, in detail, the terms and conditions of the project. Since that time, progress with the Dalkia consortium has been slow and some work remains incomplete.
17. In addition, the economic and regulatory landscape has changed significantly since the Council started the MUSCo partner procurement process. This has had an impact on the scope of the MUSCo scheme and the Dalkia's consortium's proposals as well as the Council's financial and economic position.
18. The June 2008 report to the Major Projects Board recommending approval of the Dalkia consortium as preferred bidder for the MUSCo recognised that should there be difficulties in concluding the negotiation of the project agreement the project team should return to the Board to seek guidance for the continuation of the process. In the absence of the Projects Board and as this represents the conclusion of a strategic procurement this report is brought to the Cabinet for decision.

### **Commercial Partner Process**

19. In February 2003 the Council adopted a development framework for the Elephant & Castle in the form of Supplementary Planning Guidance (SPG). The SPG promoted a

mixed use development of 6.5 million sq ft of new development. In the document it is noted that on the basis of a business as usual approach to the redevelopment that CO2 emissions attributable to domestic and non-domestic buildings would more than double. In the SPG the Council proposed to use the redevelopment as an opportunity to introduce and adopt a range of innovative measures to minimise energy consumption. To facilitate this the Council adopted a zero carbon growth strategy within the confines of the Elephant and Castle framework area and proposed the establishment of a private/public joint venture company - Environmental Services Company (ESCo) as it then was - as a special purpose vehicle whose core business would be the provision of heating, cooling and power at a community/district level.

20. Following the decision to adopt the SPG further technical and financial work was undertaken to further investigate how an ESCo at the Elephant and Castle could most practically be implemented. Initially the view taken was that this could best be achieved by integrating the procurement of energy and environmental services into the selection of the commercial partner process. This was the approach taken at the stage 2 of the commercial partner process in June 2005. Parties bidding for that role were required to provide a detailed summary of their funding and technical/management expertise in relation to provision of energy, water and data services.
21. The March 2006 report to the Executive concerning the terms for the Stage 3 commercial partner selection noted however that a review of the available options for delivery had concluded that "a separate procurement exercise for the establishment of a Multi Utility Services Company (MUSCo) is desirable. Such a company would be capable of developing the necessary infrastructure in advance of the main development programme." It was further noted that "The MUSCo proposal is an innovative one. There is no "off the shelf" model that can form the basis of the procurement process and the Elephant MUSCo will therefore need to be established on a basis that meets the demands of local circumstances". Executive were advised that further details on the proposed separate procurement approach will be brought forward as soon as possible.

### **Gateway 1 Process**

22. In July 2006 the Council formally embarked on the process of procuring a commercial partner to form a MUSCo by way of a Gateway 1 report agreed by the Executive. The company was 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 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 supplementary guidance". The emphasis in the Gateway 1 report was therefore on the provision of a MUSCo for the Elephant and Castle. The report did note that following the decision by the Council's Executive committee in September 2005 to demolish the Aylesbury estate in stages that this redevelopment "could represent an early opportunity for the extension of MUSCo services".
23. The Gateway 1 report stated that the original preference had been for an integrated commercial partner and MUSCo selection process. The report noted however that "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 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 need to capture early development was identified as an important objective in order to achieve net zero carbon growth for the Elephant and Castle redevelopment. This requirement was reflected in the procurement project plan in the report which set a planned date of May 2007 for the

Gateway 2 report to award the contract and July 2007 for the commencement of the contract.

24. In summary the Gateway 1 report identified the services that were to be provided by the MUSCo were as follows:
- A comprehensive district network delivering heat and electricity to the development.
  - A non-potable water network.
  - An open access fibre optic communications network.
  - The scope to explore the feasibility of the inclusion of other services such as mechanised waste removal and cooling.
  - Delivered as a services concession over thirty-five years.
  - The Council granting leases and way leaves to facilitate the scheme.
- Preferred sites for the location of energy centres were identified as a plot to the north of St Mary's Churchyard and the location of the current Heygate boiler house.
25. In setting out its specific requirements for the scheme the Council noted the "central drivers and objectives of this procurement process and the subsequent delivery of multi-utility services to the Elephant and Castle" and included:
- Maintaining carbon emissions at their current levels, despite almost tripling the quantum of available commercial and residential floor space - i.e. net zero carbon growth.
  - Reducing Carbon emissions from the total energy needs (heating, cooling and power) of the development by at least 10% by a combination of:
    - i. renewable energy generation at the energy centres, using locally derived sources of renewable fuel,
    - ii. Building mounted/integrated renewable energy technology within development plots.
  - Reducing the demand for potable water by 20% at the point of supply and provide an alternative source of untreated water for the non-potable uses associated with construction, operation and maintenance of the development.
  - Delivering a "Fibre to the Unit" network to provide robust, sustainable optical fibre based connectivity to every address point within the core development area, and the early housing sites.
  - Establishing a public/private joint venture vehicle (MUSCo) as a special purpose vehicle whose core business is the provision of low carbon heating, cooling, power, non-potable water and data services at district level.

### **Response to MUSCo Invitation**

26. In response to the publication of an OJEU contract notice the Council received expressions of interest from fifteen organisations. Three consortia subsequently submitted tenders. All three consortia were short-listed and following Executive approval on April 24 2007 each was invited to a third, Best and Final Offer (BAFO) stage of the procurement process.
27. Stage 3 of the MUSCo process was delayed whilst the Council appointed a preferred bidder in July 2007 for Master Development Planner for the Elephant and Castle who would be able to participate in the MUSCo selection process.
28. This stage of the MUSCo bid was an iterative process with a series of briefings and workshops on each of the key subject areas for the submissions. Following the establishment of a set of core principles for the project agreement and joint working between selection and financial close bidders were each requested to submit a Best and Financial Offer (BAFO).

29. BAFO proposals were received on May 6 2008. On June 19 2008 the Major Projects Board agreed to select the Dalkia consortium “as its preferred MUSCo commercial partner to final negotiation stage based on the terms included in the invitation to submit a best and final offer and response to that document”.
30. Technically the Dalkia consortium presented robust and comprehensive proposals that demonstrated a considerable breadth and depth of knowledge and expertise in delivering CHP led production of three energies: electricity, heat and chilled water solutions. It also provided useful additional information on energy centre and networks operation, site monitoring and plant management.
31. The Dalkia consortium bid proposed the establishment of a Special Purpose Vehicle which would subcontract the MUSCo services. Dalkia itself is owned by Veolia Environment as majority shareholder and EDF. Dalkia is a significant company in its own right with over 50,000 employees and annual revenue of £6.8 billion.
32. The Board further instructed officers “to proceed with detailed negotiations to complete the full contractual documentation that would give effect to the proposed joint working arrangements acceptable to the Council subject to final approval of the project agreement and associated documentation at the contract award (Gateway 2) stage”. The report noted that whilst negotiations would continue neither party were obliged to enter into contract.

#### **CHANGES TO ORIGINAL VISION SINCE THE PROCUREMENT PROCESS STARTED**

33. The MUSCo procurement process which commenced as a separate entity in 2006 has been significantly delayed by a number of factors including the following:
  - The lengthy negotiations with Lend Lease as the Master Development Planner for the Elephant and Castle regeneration.
  - The impact of the economic downturn leading to Lend Lease delaying both the roll out of their construction programme and significantly reducing their projected build-out rates for new housing have all played a part in reshaping the scheme.
  - The publication of the Area Action Plan for the Aylesbury Estate leading to the reshaping of the MUSCo energy services and water services strategies, resulting in a revised technical and commercial approach to the delivery of plant and infrastructure.
  - Changes in planning policy and building control standards which have led to more demanding carbon reduction targets and building efficiency standards.
34. A summary of the key dates associated with the process illustrating how far it has been set back is shown below:

## Background to MUSCo / Outline process to date

Date	Activity
2003	<ul style="list-style-type: none"> <li>• Environmental impact analysis of development of E&amp;C – energy, carbon emissions, water and waste.</li> <li>• Target of zero growth in emissions proposed – with development increasing building floor space by 300%.</li> <li>• Technical options appraisal – district heating and CHP identified as most cost effective route.</li> </ul>
2004	<ul style="list-style-type: none"> <li>• Zero carbon growth target adopted for Elephant and Castle along with proposal to establish delivery vehicle 'Energy Services Company' (ESCo)</li> </ul>
2005	<ul style="list-style-type: none"> <li>• Master Development Planner selection. ESCo responses from bidders unsatisfactory.</li> <li>• Market testing for potential bidders for separate 'Multi Utility Services Company'.</li> </ul>
July 2006	<ul style="list-style-type: none"> <li>• Approval of Gateway 1: Procurement Strategy Report</li> </ul>
October 2006	<ul style="list-style-type: none"> <li>• Stage 2 of the procurement process is launched with the focus on the Elephant and Castle and Aylesbury estates with the option of expanding overtime. Two energy centres were to be sourced one at St Mary's Churchyard the other at Heygate.</li> </ul>
March 2007	<ul style="list-style-type: none"> <li>• Three bidders chosen to enter Stage 3 - Dalkia, London ESCo and Thamesway.</li> </ul>
July 2007	<ul style="list-style-type: none"> <li>• Lend Lease appointed Elephant and Castle preferred Master Development Partner but economic downturn delays progress.</li> </ul>
May 2008	<ul style="list-style-type: none"> <li>• Dalkia selected PB with only St Mary's selected as a site</li> </ul>
January 2009	<ul style="list-style-type: none"> <li>• Lend Lease inform Council of major delay to Elephant and Castle scheme and revise development phasing. Information passed to Dalkia to update their offer.</li> </ul>
September 2009	<ul style="list-style-type: none"> <li>• Dalkia response to move to Heygate and create a "Biomass power station", biomass boiler in Aylesbury and gas fired boilers at Newington.</li> </ul>
	<ul style="list-style-type: none"> <li>• Key meeting and decision that Heygate could not accommodate plant of scale and massing as proposed. Mandela Way site suggested by the Council.</li> </ul>
November 2009	<ul style="list-style-type: none"> <li>• Proposed move of the Energy Centre to Mandela Way.</li> </ul>
February 2010	<ul style="list-style-type: none"> <li>• Outline commercial structure from Dalkia for latest project submitted.</li> </ul>
July 2010	<ul style="list-style-type: none"> <li>• Revised BAFO submitted which is now supplying heat to the Elephant and Castle and the new and existing housing estates at Aylesbury, Newington, Salisbury and Heygate.</li> </ul>
20 September 2010	<ul style="list-style-type: none"> <li>• Responses submitted to Clarification Questions</li> </ul>
14 October 2010	<ul style="list-style-type: none"> <li>• Dalkia presentation to senior managers</li> </ul>

## KEY ISSUES FOR CONSIDERATION

### Current Position / Negotiation process

35. The impact of these events has led to considerable changes in the nature and shape of the MUSCo proposed by the Dalkia consortium as it took stock of its offer and considered the impact on the technical solution and business plan originally proposed as part of its bid. The original approach to the deployment of the MUSCo network was premised on the construction and occupation of new development on both the Heygate and other private/Registered Social Landlord (RSL) schemes close to the centre of the Elephant and Castle by 2010. The delay in bringing forward the critical mass of new development which would have been necessary to support the Dalkia consortium's original proposals during the intervening period is an important underlying factor when considering the future of the procurement process.
36. At this point the Dalkia consortium changed the emphasis of their approach from one which centred on a MUSCo for the Elephant and Castle with the potential to expand to connect to other areas to one more focused on early supply of heat to the Aylesbury which would enable investment to be released for a district wide system that had the capacity to connect to the Elephant and Castle when phases of development were complete.
37. In spring 2009 officers met with the Dalkia consortium to further investigate the proposals. The primary focus of this work was the evaluation of the design of the much larger boiler house for the redevelopment of the Heygate estate. In September 2009 an internal review by Council officers and technical advisers concluded that the scale and potential environmental impacts of the Dalkia consortium's proposal for an energy centre on Heygate would, given the close proximity of existing and proposed residential development, make it unacceptable on planning and commercial grounds. This would be exacerbated by the associated frequency of biomass fuel deliveries.
38. Alternative locations away from the Heygate site were therefore considered and this resulted in a site at Mandela Way being identified as a potentially more suitable location for the energy centre, subject to the usual planning and development control processes. Further technical and design work was undertaken to test the potential of this site to accommodate a biomass energy centre and to evaluate the planning implications and impact on adjoining residents. This identified issues such as noise and vibration that would need to be assessed further to establish whether they could be sufficiently mitigated to meet planning and environmental health policy and standards.
39. In March 2010, the Council issued a "checklist of requirements" requesting further clarity from the Dalkia consortium on its proposed technical and commercial solutions for a MUSCo proposal based on a biomass energy centre based at Mandela Way. In addition the checklist sought to advance negotiations with the consortium towards a full project agreement, with the aim of achieving approval to enter into contract by the end of 2010.
40. The Dalkia consortium submitted a revised technical and commercial offer of services on 2 July 2010. This was followed by a round of clarification questions and technical workshops which concluded on 20 September 2010 with the submission of a co-ordinated clarification response from the Dalkia consortium.
41. The Dalkia consortium gave a presentation on their proposals to a team of senior officers and consultants on 14 October 2010.

## **DALKIA'S FINAL PROPOSALS**

42. The evaluation of the Dalkia consortium's final proposals including its revised BAFO and subsequent responses to the Council's clarification questions was undertaken by a core officer team comprising the Strategic Director of Environment and Housing, Finance Director, Project Director - Elephant and Castle, acting Head of Sustainable Services, and the Head of Environment and Housing Procurement. The Dalkia presentation was also attended by the Head of Property and the Aylesbury Programme Director. The Council was also supported by external legal, technical and financial advisers.

### **Technical Proposals**

43. The Dalkia consortium's technical proposal includes key elements of plant and infrastructure which are detailed more fully in the closed report. The proposals include a number of changes to the technical solution submitted previously including the following:
- A move from heat sales as the commercial driver for the energy model to electricity export sales and renewable obligation certificates.
  - A move from gas-fired combination heat and power (CHP) to biomass CHP.
  - A significant increase in the scale of on-site electricity generation plant.
  - Use of waste wood as the primary fuel for the biomass CHP plant.
  - A significant increase in the number of lorry deliveries to the CHP plant.
  - The extension of MUSCo water services to include potable water and wastewater services.
  - A move from borehole water to treated wastewater as the source of non-potable water across the Elephant and Castle / Aylesbury area.
  - The use of boreholes drilled by the Council as a backup supply for the non-potable system.
44. The technical proposal includes key elements of plant and infrastructure which are discussed in more detail below.

### **Energy Plant**

45. The energy plant would comprise the following:
- A biomass combined heat and power plant (wood chip boiler and steam turbine) would be built at Mandela Way.
  - A new boiler house on the Aylesbury Estate.
  - A new boiler house on the corner of Heygate Street and Rodney Road.
  - Replacement of two existing boilers at Newington boiler house.
46. The revised BAFO delays the deployment of the new gas boilers to the Newington boiler house to 2014 and to the Heygate boiler house to 2020. The completion date for the biomass energy centre is scheduled for commissioning in late 2012.
47. Woodchip would be delivered to Mandela Way by two 24t articulated trucks delivering every hour between 8am and 5pm Monday to Friday. The energy centre would run 24 hours a day. The plans show that the tallest and noisier elements of the plant would be located as far away from neighbouring residential property as possible within the confines of the site.

### **District Heating Network**

48. A low temperature hot water district heating network would be provided with proposed heat charges to the tenants combining both a fixed service charge and a floating



charge based on usage and modelled on the basis that rates are below benchmarkable gas rates obtainable from a recognised energy comparison site.

### **Potable and Non-Potable Water**

49. Veolia Water would provide potable and non-potable water services.
50. They propose to seek OFWAT approval to provide potable water purchased from Thames Water and resold to customers within the area.
51. For non-potable water, provided for toilet flushing, irrigation, public area cleansing and building water, Veolia Water propose to adopt one of two potential wastewater treatment technologies – a more traditional Membrane Bioreactor (MBR) wastewater plant or an Organica plant, which uses metabolic processes of living organisms – plants, animals and microbes - that digest organic pollutants to treat wastewater. The MBR is more energy intensive and less aesthetically pleasing whilst the Organica has a higher capital cost and larger footprint. The location of the wastewater treatment and reuse plant is to be determined though Veolia Water have suggested that Elba Place and some surrounding park land could be utilised.
52. Veolia Water proposes to use a borehole at Brook Drive to supply non-potable water to early housing sites and to provide a back-up supply for the re-use plant once online.
53. Water tariffs would be set below that of the current incumbent e.g. Veolia Water estimate an annual saving of around £90 based on a 2 bedroom flat.

### **Fibre Optics**

54. An integrated, future-proofed telecoms infrastructure would be provided to deliver voice, data and television networks to users. Charges would be at or below current UK prices. Residents would be able to request a BT connection if they are dissatisfied with the price or quality of the service on offer.

### **Project Co-ordination**

55. All utility networks would be designed to occupy a single trench aiming to minimise on-site disruption where practicable.

### **COUNCIL CONSIDERATION OF DALKIA'S PROPOSALS**

56. In April 2010 the Dalkia consortium was sent a comprehensive checklist of the information required to secure Gateway 2 approval for the Council to enter into a Project Agreement for the provision of MUSCo services. This updated the requirements checklist that had been sent to all bidders at the start of the BAFO process in April 2008.
57. The 2010 checklist stated explicitly that the revised BAFO should contain a sufficiently comprehensive and detailed description of the technical, financial and legal operation of the MUSCo, and its contractual relationship with key stakeholders going forward, to conclude contract negotiations in a timely fashion.
58. Clarification was sought from the Dalkia consortium regarding outstanding issues in September 2010.
59. Having reviewed the totality of the Dalkia consortium's BAFO submissions against the information they had been asked to supply, the Council's officer team have a number of outstanding concerns. The details of these concerns are set out in the closed report. In summary the concerns centre around the following issues:

### **Funding proposal**

60. There is a lack of certainty around the Dalkia consortium's financing arrangements which creates uncertainty with respect to the viability of its proposal as a fully funded MUSCo solution.

### **Risk transfer**

61. The Dalkia consortium is no longer willing to take on full commercial, build and load risks it had proposed in its original submission.

### **Financial model**

62. The Dalkia consortium has to date only released a partial financial model with too little information to allow any meaningful analysis to be undertaken.

### **Heads of Terms/Project Agreement**

63. The heads of terms for the project agreement are yet to be agreed.

### **Parent Company Guarantee**

64. There is a lack of certainty regarding the parent company guarantees will ultimately be forthcoming.

### **Mandela Way proposals**

65. On the basis of the information provided, the Council has not been able to conclude that the power plant proposed by the Dalkia consortium on Mandela Way is viable and likely to proceed successfully. There is therefore a risk that the Dalkia consortium will be unable to deliver a viable MUSCo solution to the development area without investing further time and resource into formulating an alternative heat proposal. This is likely to create further delay to the deployment of the MUSCo scheme.

### **Delivery programme**

66. The Dalkia consortium has not supplied a phased development plan setting out key assumptions in relation to activities, interdependencies and anticipated delivery dates for achievement of milestones and facilities coming on stream in relation to the MUSCo project.
67. In the absence of a phased development plan, the Council is not in a position to assess either the reasonableness of any assumptions that have been made in the revised BAFO, or the relationship between the development programme at Aylesbury, Elephant and Castle and the MUSCo. The negotiation of an agreed phase development plan and project agreement is likely to involve further delay to the MUSCo project. There is a risk that this delay may also have a further negative impact on the overall Elephant and Castle development timeline.

### **Conclusion**

68. Whilst the Dalkia consortium's technical proposals have merit, for the reasons set out in the closed report, officers are unable to recommend acceptance of the Dalkia consortium's BAFO.

69. The Dalkia consortium has not provided adequate responses to some critical questions and there is insufficient evidence to be able to conclude the proposed arrangement represents value for money to the Council.
70. Officers consider that further discussions with Dalkia are unlikely to yield an agreement within the timeframe required to complete the process without impacting negatively on the wider regeneration schemes. Overall the proposals represent a high degree of uncertainty and potential risk to the Council. There is insufficient evidence for officers to be able to conclude that the proposed arrangements represent value for money. Officers are not persuaded that allocating further time and cost to resolving outstanding issues would result in a satisfactory outcome within a timeframe required to complete the process without impacting negatively on the wider regeneration schemes.

## **ALTERNATIVE SOLUTIONS / NEXT STEPS**

### **Elephant and Castle**

71. Under the terms of the Regeneration Agreement should the MUSCo not proceed Lend Lease are under an obligation to work together with the Council to establish an alternative solution. An alternative solution would need to satisfy planning policy requirements for sustainability/carbon reduction as set out in the London Plan, Southwark Plan/Core Strategy, relevant SPD's as well as building control requirements for energy efficiency. An opportunity area planning framework is being prepared for the Elephant and Castle and this will provide further guidance on the sustainability requirements that Lend Lease will be expected to comply with. In addition under the Regeneration Agreement a condition precedent is the provision of a MUSCo.
72. Lend Lease remain committed to delivering the sustainability obligations within the Regeneration Agreement and the associated conditions. As part of the master planning process Lend Lease are considering options to deliver a sustainable development. This includes a review of the onsite provision of CHP / District Heating, non-potable water and Enact [mechanical waste removal systems]. These matters need to be considered in terms of the masterplan and the commercial appraisal to determine the viability for the development. A Lend Lease only solution will however be an additional cost to the scheme. Although this will not impact on the base land value that the council is entitled to receive it could have an adverse affect on future profit share.
73. The Lend Lease alternative approach is likely to be a commercially operated energy centre (an Energy Services Company [ESCO] providing heat to buildings within their boundary of their planning consent. Lend Lease will investigate alternative solutions and are seeking an outcome which will aim to achieve Code Level 6 of the Code for Sustainable Homes from 2016. This marks the highest level of sustainability incorporating the Government's zero carbon home standard. Such a plant would only become commercially viable once a critical mass of development has been reached (probably in the region of 800 -1000 units). Early phases of development would therefore have to be designed to have the capacity to connect to the system once it comes on stream.
74. The evidence to date from technical work the Council has undertaken suggests that it is likely that the building footprint for this facility will be larger than that required for the Dalkia consortium's MUSCo proposals. It is possible that the Lend Lease facility may have the capacity to supply other sites outside their planning boundary close to the heart of the redevelopment area including some that were designed to connect to the MUSCo. The heating load arising from these developments could potentially improve the business case for an ESCo located within the Lend Lease site and this might allow the facility to be developed earlier than would be the case if only developments within the

red line boundary of the Lend Lease scheme are connected to it. The extent to which this is practical is being explored with Lend Lease.

75. In addition Lend Lease will need to identify land for water recycling and treatment and also for electrical sub station as part of the reinforcement works necessary to upgrade infrastructure to cope with the demands arising from an increasing population. The land for all these facilities will need to be identified within the planning application. Appropriate measures will need to be put in place to mitigate potential adverse affects arising from noise, vibration, air quality associated with the plant on adjoining land uses.

## **Aylesbury**

76. The MUSCo proposal included siting a new district heating facility on the Amersham development site (Site 10) in the Aylesbury Area Action Plan (AAP). It is understood that this facility was intended to replace the existing district heating plant on an adjacent site immediately south to the Amersham site. The decision to include a new district heating facility on the Amersham site resulted in the Council having to depart from the AAP by relocating the Medical Centre that was due to be included on this site elsewhere. If the MUSCo proposal fails to proceed then the council would be in a position to revert to the AAP and locate a Medical Centre on the Amersham site in addition to the community space/facilities that are prescribed in the AAP for the Amersham site. In addition, it would also allow Council officers to review the options for:

- Continuing to provide heating to the existing homes on the Aylesbury Estate.
- Helping the council's developer partners meet the requirements of Level 6 of the Code for Sustainable Homes.
- Making better use of the current Council owned and operated energy centre.

77. Council officers are currently procuring the services of expert consultants to assist with identifying the range of management options, evaluating them and making recommendations on the best value option and expect to report back to Cabinet on these matters in due course. It should be noted, however, that the options to be brought forward to Cabinet may not necessarily include the broad range of services currently being offered by the MUSCo, such as data, power and water services.

78. An added complication to the delivery of the Aylesbury Regeneration Programme is the recent press announcements by CLG (Department for Local Government & Communities) and the HCA confirming the curtailment of PFI funding for 'pipeline' PFI Housing Projects (i.e. projects that have not had their business cases approved by HM Treasury's Project Review Group). The immediate implications for the Aylesbury Regeneration Programme are that the:

- redevelopment of sites comprising the Aylesbury PFI Housing Project (sites 1b, 1c, 8 & 9) comprising Bradenham, Arklow, Chartridge, Chiltern, Taplow and Northchurch is likely to be delayed
- income to the Council from its Aylesbury Infrastructure Tariff (a charge paid to the council generally on the homes for sale) will be delayed.

79. Delays and/or reductions to the Aylesbury Infrastructure Tariff cash-flow means that the Council may not have the resources to fund the provision of improved district heating and other tariff funded items resulting in the postponement of the implementation of some tariff items, such as district heating solutions.

## **Southwark CHP (SELCHP Project)**

80. Officers are bringing forward a proposal, also on this agenda, to seek to connect almost three thousand Southwark Council properties to the South East London Combined Heat and Power (SELCHP) plant in north Lewisham in order to provide them with a more energy efficient supply of heating and hot water using heat that is currently wasted at the SELCHP plant. Initially the project will work to deliver that heat supply to properties on five estates in the north east of the borough, close to the SELCHP plant. However, after supplying heat through the north eastern branch there will still be a substantial amount of heat still available (and wasted) at SELCHP. Once the heat distribution infrastructure is in place there could be scope for the scheme to expand to link to other housing stock and commercial premises in other parts of Southwark, subject to economic and heat distribution infrastructure constraints. Options could therefore be considered to extend the heat distribution infrastructure as part of, or subsequent to, the current Southwark CHP project.

### **Policy implications**

### **Other considerations**

81. There are no specific leaseholder implications arising from this report.

### **Sustainability considerations**

82. The burning of fuels to generate electricity and heat, or power travel, emit large amounts of carbon dioxide into the atmosphere, which is a key contributor to gradual climate change and an increase in extreme weather conditions around the world.
83. The Climate Change Act 2008 sets binding carbon emission reduction targets for the UK. While the current UK regime of indicators and targets is currently under review, Southwark Council, like all local authorities in the UK, will face challenging carbon reduction targets in the coming years. Through leading partnership plans, developing planning strategies and agreeing sustainability as a corporate objective, the Council has consistently committed to be a champion of sustainable development.
84. 84% of Southwark's carbon emissions are understood to originate from the built environment. The MUSCo had been identified as a significant element of a set of complex projects that would help support reduction of emissions by 60,000 tonnes of CO<sub>2</sub> and develop carbon efficient infrastructure throughout the borough.
85. The Council has adopted a zero carbon growth strategy within the confines of the Elephant and Castle framework area and, in accordance with the London Plan, a major part of this must be through the use of renewable sources of energy and low-carbon technology. Alongside efficient design to reduce energy requirements, the MUSCo represented a major contribution to reducing emissions associated with the development. In addition, the MUSCo scheme would have provided for energy generation of at least 20% renewable by a combination of renewable energy generation at the energy centres and building and locally based renewable technology. It would have also reduced the demand for potable water.
86. The Council remains a committed champion of sustainable development and the 2006 Climate Change Strategy sets out the Council's aims to reduce CO<sub>2</sub> emissions across the borough by 80% by 2050 and to pursue a decentralised energy strategy. The approach taken in the Core Strategy which applies to all development within the borough is in line with London Plan policies which expect development to meet the highest standards of sustainable design and construction and to help tackle climate change by applying the energy hierarchy of implementing energy efficiency measures, ensuring efficient energy supply and making use of renewable and low carbon sources of energy. These policies are being implemented within the Aylesbury

Regeneration Programme. Furthermore, the zero carbon growth strategy within the confines of the Elephant and Castle is retained (subject to the Elephant and Castle SPD) as is the London Plan requirement to reduce carbon emissions by at least 20% through using on-site or local low and zero-carbon sources of energy. Therefore the Council and its partners will have to look at alternative ways to achieve these same outcomes. As with the MUSCo approach, this is likely to be achieved through a mixture of measures including energy efficient design, minimising water use and utilising local sources where possible, local renewable energy generation and combined heat and power schemes. In addition this report recommends that the Council's housing management service look into the feasibility of further decentralised energy networks and the pursuit of the project to utilise renewable heat in Council housing estates using heat from the SELCHP plant. These projects - at the Elephant and Castle, on the Aylesbury, SELCHP and in social housing will seek to maximise contribution to reducing carbon emissions and redress the impact of not pursuing the MUSCo option.

87. During the development of proposals for the Elephant and Castle, emphasis has been placed on the sustainability of the scheme in terms of energy use and carbon emissions. This emphasis was given weight when the Clinton Foundation, an international body seeking to grow capacity to meet the challenges of global interdependence, named the Elephant and Castle project as a founding scheme in its Climate Positive Development Program. This initiative aims to support the development of large-scale urban projects that demonstrate cities can grow in ways that are "climate positive." Following a meeting with the Clinton Foundation they confirmed that in the eventuality that the MUSCO did not proceed they would still support the Elephant and Castle project as long as the key sustainability targets remained in place. The Council remains clear that it continues to prioritise sustainability regarding energy use and carbon emissions in new development and as set out above, while the Council proposes to terminate the MUSCo procurement, its objectives with respect to minimising climate impact through the Elephant and Castle development remain unchanged.

### **Staffing implications**

88. There are no specific staffing implications arising from this report.

### **Financial implications**

89. Detailed consideration of the financial issues relating to the Dalkia consortium's final proposals are set out in the closed report.
90. The cost of the managing the MUSCo procurement and contract negotiation process including fees for external advisers was met from the Elephant and Castle Development team's revenue budget with contributions from earmarked reserves from 2006/07 until 1 September 2010 when responsibility for the project transferred to Environment and Housing. In stopping the project the Council will not continue to use resources on a project that is not viable. Furthermore the work undertaken to date is not wasted and will still contribute to the Elephant and Castle and other development projects across the borough.
91. Were the procurement to proceed future revenue and capital costs would be needed to be identified.
92. Costs of alternative solutions will need to be reviewed once detailed proposals are known, all of which will need to be subject to business cases to be agreed by the Cabinet.

### **Legal implications**

93. The legal implications are set out in the concurrent report of the Strategic Director of Communities, Law & Governance in the closed report.

### **Consultation**

94. Lend Lease was part of the original evaluation team that selected the Dalkia consortium as preferred bidder. The company was also part of the group to whom the Dalkia consortium gave their presentation in October 2010.
95. Whilst there was consultation with strategic bodies such as the Mayor's Office and the LDA regarding the proposals for the MUSCo, there has not been any further discussion with them concerning the possibility of ending the Dalkia consortium's role of preferred bidder nor of stopping the procurement of a MUSCo altogether.

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

#### **Strategic Director of Communities, Law & Governance**

96. This report seeks the cabinet's approval to a number of recommendations in relation to the MUSCo project, including the termination of Dalkia as preferred bidder. As this is the conclusion of a strategic procurement, the approval of these recommendations is reserved to the cabinet.

#### **Finance Director**

97. The Finance Director notes the recommendations included in this report and supports the rationale for suspending the current procurement as outlined.
98. The Council will need to continue to support future initiatives to achieve the original objectives of the MUSCo procurement as amended to take account of feasibility, timescales, technologies, external targets for delivery. Costs will be financed as previously through a combination of revenue budgets, capital contributions and allocations from earmarked reserves, both General Fund and HRA.

#### **Head of Procurement**

99. The MUSCo procurement has been undertaken over a significant period of time with unusually long delays between phases and set against a back-drop of economic, financial and regulatory change. External factors identified in the report have played a part in the Dalkia consortium recasting its original proposals and ultimately submitting a much altered final BAFO.
100. The report confirms that the Council has clear reasons for not continuing with the procurement process. The Dalkia consortium's bid itself has failed to meet the Council's requirements in a number of critical areas and the proposals lack the detail needed to demonstrate that value for money is being obtained. The evaluation team consider there is no evidence to suggest that allowing further time for the process would result in a satisfactory outcome within a timescale compatible with the needs of the Council's wider regeneration schemes.
101. The report notes that it has been established throughout the procurement process that there was no certainty that an agreement would be reached for the MUSCo and that there was a recognised risk that a contract may not be awarded. The risks associated with the proposed termination of the process are detailed.
102. This has been a complex procurement process with valuable lessons which should be captured and shared for all major procurements. Appropriate governance arrangements

should be established for any related procurements taken forward as alternative solutions to providing services and reducing carbon for the Elephant and Castle and Aylesbury regeneration projects and the decentralised energy networks for Council social housing.

## BACKGROUND DOCUMENTS

Background Papers	Held At	Contact
2 <sup>nd</sup> Deposit Southwark Plan and E&C SPG adopted February 2004	160 Tooley Street, SE1 2TZ	Jon Abbott x 54902
MUSCo Gateway 1 - July 18 2006	160 Tooley Street, SE1 2TZ	Jon Abbott x 54902
MUSCo PSP Tender Documentation	160 Tooley Street, SE1 2TZ	Jon Abbott x 54902
Climate Change Strategy	160 Tooley Street, SE1 2TZ	Energy Team x 53804

## AUDIT TRAIL

<b>Cabinet Member</b>	Councillor Fiona Colley, Cabinet Member for Regeneration and Corporate Strategy		
<b>Lead Officer</b>	Gill Davies, Strategic Director of Environment and Housing		
<b>Report Author</b>	Mike Green, Head of Environment and Housing Procurement		
<b>Version</b>	Final		
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<b>Key Decision?</b>	Yes	<b>If yes, date appeared on forward plan</b>	January 2011
<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / CABINET MEMBER</b>			
<b>Officer Title</b>	<b>Comments Sought</b>	<b>Comments included</b>	
Strategic Director of Communities, Law & Governance	Yes	Yes	
Finance Director	Yes	Yes	
Head of Procurement	Yes	Yes	
<b>Contract Review Boards</b>			
Departmental Contract Review Board	Yes	Yes	
Corporate Contract Review Board	Yes	Yes	
<b>Cabinet Member</b>	Yes		
<b>Date final report sent to Constitutional Team</b>			13 January 2011