

Committee: Cabinet

Date: 25 March 2019

Wards: All

Subject: Extension of Contracts for Supply of Electricity and Gas

Lead officer: Caroline Holland, Director of Corporate Services

Lead member: Councillor Mark Allison

Contact officer: Richard Neal, Energy & Sustainability Manager

Recommendations:

- A. Confirm the Extension of the Contract for The Supply of Electricity with Scottish Power for a further year until 31/03/22, at an estimated cost of £1.7m
 - B. Confirm the Extension of the Contract for The Supply of Gas with Gazprom for a further year until 31/03/22, at an estimated cost of £0.75m
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1 PURPOSE OF REPORT AND EXECUTIVE SUMMARY

- 1.1. The Council is in delivery year 2 of 4-year flexible supply contracts with its electricity (Scottish Power) and Gas (Gazprom) suppliers, and officers are seeking approval to take up 1-year extensions to both contracts.
- 1.2. Exercising the 1-year extension options needs to be confirmed as a key decision as the annual value of each contract is in excess of £500,000.

2 DETAILS

- 2.1. The Council awarded contracts for the supply of electricity to Scottish Power, and gas to Gazprom in April 2017. The award was made subsequent to confirmation of the outcome of an OJEU compliant tender process at the 13th February 2017 Cabinet meeting.
- 2.2. Under current arrangements the contracts with both suppliers will end on 31/03/21, but both contain an optional 1-year extension option.
- 2.3. Volumes of power / gas for delivery via these supply contracts are purchased on the wholesale market by the council's Independent Energy Consultant, Kinect Energy. Only volumes relating to periods within a current supply contract can be purchased, meaning Kinect can only currently trade energy (and attempt to secure optimal pricing) for delivery up until 31/03/21.
- 2.4. Due to the nature of these contracts – i.e. the exact prices and consumptions are not known ahead of time – it is impossible to state with certainty the value of the additional year. However at the point of contract award annual values were estimated as;

The electricity supply contract was estimated to be £2,000,000 p.a.

The gas supply contract was estimated to be £1,500,000 p.a.

- 2.5. Actual spend on the contract to date has come in below the initial estimates, with electricity spend approximately £1,700,000 annually, and gas £750,000 annually. A combination of low wholesale prices at the start of the contracts, extensive energy saving works across the portfolio, and a degree of over estimation account for these savings.
- 2.6. Officers are seeking to extend the contracts until 31/03/22 at this time for a number of reasons;
- i. Market movements. The market has been very volatile over 2018/19, but equally has been moving predominantly upwards. As a result, the longer the council postpones purchasing volumes for the additional year the greater the change in prices we will see when we move out of the initial term.
 - ii. Purchasing Strategy. Keeping open a three year rolling purchasing window is generally recommended with flexible supply contracts. This provides a balance between achieving best price, providing access to periods in the market with sufficient liquidity (there tend to be little liquidity in the market beyond three years out).
 - iii. Forward planning. By extending now, it gives the Council the ability to run the tender for the next electricity and gas supply contracts suitably in advance of delivery so that subsequent volumes can be managed in line with its current trading strategy. By doing any new tenders at the last minute the council would effectively be in the same situation as if it extended existing contracts towards the end of the current initial term.
 - iv. Market Engagement. Only Gazprom submitted a bid during the last Gas Supply procurement exercise. Earlier extension of this contract will enable officers to begin early engagement with the market with a view to ensuring a greater number of responses the next time these services are tendered for.
- 2.7. Performance by the incumbent suppliers on both contracts has been good, and while the Council is in delivery year 2 of the current contracts, both suppliers have actually been in place under similar terms for a total of 7 years. As such the likelihood of an unacceptable deterioration in their performance is considered remote.
- 2.8. The risk of deterioration in performance is therefore considered to be outweighed by the market risk of not being able to buy volume for the additional year significantly ahead of point of delivery.

3 ALTERNATIVE OPTIONS

- 3.1. The decision on whether to extend the supply contracts could be left until nearer the end of the initial term. While this would enable the Council to exit its current arrangements in 2021, it would increase the risk of it being exposed to Market volatility during 2021/22.
- 3.2. Supply contracts could be re-tendered at this time for a 21/22 start date. While this would provide the longest purchasing window (e.g. until 2024/25) there is little additional value in being able to purchase beyond a three year window, and the administrative burden placed on officers would be significant.

4 CONSULTATION UNDERTAKEN OR PROPOSED

- 4.1. The recommendation to exercise the option to extend these contracts was approved at the 11/12/18 Procurement Board meeting.
- 4.2. The decision to award of the supply contracts was confirmed at the 13/02/17 Cabinet meeting.

5 TIMETABLE

- 5.1. Approval to proceed from Procurement Board – 11th December 18
- 5.2. Report to Cabinet for Key Decision approval – 18th February 19
- 5.3. Notification to Suppliers of Contract Extension – 19th February 19 (note no standstill applies as this is an extension to an existing contract)

6 FINANCIAL, RESOURCE AND PROPERTY IMPLICATIONS

- 6.1. Extension of the supply contracts will increase the Council's ability to achieve best value by both allowing a longer purchasing window and providing greater budget certainty.
- 6.2. Due to the nature of these contracts – i.e. the exact prices and consumptions are not known ahead of time – it is impossible to state with certainty their annual value. However at the point of award annual values were estimated as;

The electricity supply contract is estimated to be £2,000,000 p.a.

The gas supply contract is estimated to be £1,500,000 p.a.

- 6.3. Actual spend on the contract to date has come in below the initial estimates, with electricity spend approximately £1,700,000 annually, and gas £750,000 annually. A combination of low wholesale prices at the start of the contracts, extensive energy saving works across the portfolio, and a degree of over estimation account for these savings.

7 LEGAL AND STATUTORY IMPLICATIONS

- 7.1. As the extensions are provided for under the contracts there are no issues in doing so under the Public Contracts Regulations, which would apply in these circumstances due to the value of the contracts.

8 HUMAN RIGHTS, EQUALITIES AND COMMUNITY COHESION IMPLICATIONS

- 8.1. None identified.

9 CRIME AND DISORDER IMPLICATIONS

- 9.1. None identified.

10 RISK MANAGEMENT AND HEALTH AND SAFETY IMPLICATIONS

- 10.1. While providing an extended purchasing window does not eliminate purchasing risk, it does allow it to be spread and controlled through market observation and timing. A purchasing strategy of this type is generally accepted to minimise purchasing risk.

11 APPENDICES – THE FOLLOWING DOCUMENTS ARE TO BE PUBLISHED WITH THIS REPORT AND FORM PART OF THE REPORT

11.1. None

12 BACKGROUND PAPERS

12.1. None