Author/Lead Officer of Report: David Gee
Tel: 0114 273 4066

Report of: Laraine Manley
Report to: Councillor Bryan Lodge
Date of Decision: 30/03/2017
Subject: Acceptance of grant for Phase1, for the connection of the E.ON biomass plant to the SCC District Energy Network,

Is this a Key Decision? If Yes, reason Key Decision:-
- Expenditure and/or savings over £500,000
  Yes [X] No [ ]
- Affects 2 or more Wards
  Yes [X] No [ ]

Which Cabinet Member Portfolio does this relate to? Environment
Which Scrutiny and Policy Development Committee does this relate to? Economic and Environment Wellbeing.

Has an Equality Impact Assessment (EIA) been undertaken? Yes [X] No [ ]
If YES, what EIA reference number has it been given? 1250

Does the report contain confidential or exempt information? Yes [ ] No [X]
If YES, give details as to whether the exemption applies to the full report / part of the report and/or appendices and complete below:-

“The (report/appendix) is not for publication because it contains exempt information under Paragraph (insert relevant paragraph number) of Schedule 12A of the Local Government Act 1972 (as amended).”
Purpose of Report:

To allow the Council to enter into two Memorandums of Understanding (MoUs), grant agreements as part of the Heat Networks Investment Project with the Department for Business, Energy and Industrial Strategy (BEIS), along with a s.151 officer approval form.

Signing the MoUs will allow (but not require) the Council to draw down grant funding of up to £2.232 million during 2017/18 to support the cost of connecting the E.ON biomass plant at Blackburn Meadows to the SCC District Energy Network (DEN) providing an additional source of low cost, low carbon heat and facilitating the development of the SCC DEN.

An Outline Business Case (OBC) for the project is attached. SCC will act as the Accountable Body, passing the grant funding and related obligations to E.ON who will construct the connection.
Recommendations:

That the Individual Cabinet Member for Environment:

1. Approves the acceptance of the grant funding, totalling £2,231,250 from the Department for Business, Energy and Industrial Strategy (BEIS), via Salix (its agent), for commercialisation and construction.

2. Delegates authority to the Executive Director of Place to enter a Memorandum of Understanding for the commercialisation grant for £417,500 and a separate Memorandum of Understanding for the construction grant for £1,813,750 with BEIS.

Background Papers:
(In insert details of any background papers used in the compilation of the report.)

Please see OBC attached.
Please see MoUs attached.

Lead Officer to complete:-

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Lead Officer Name: David Gee
Job Title: Waste Project Director
Date: 24/03/2017
1. **PROPOSAL**

(Explain the proposal, current position and need for change, including any evidence considered, and indicate whether this is something the Council is legally required to do, or whether it is something it is choosing to do)

1.1 The proposal is to accept up to £2.232m of grant funding from the Heat Networks Investment Project, part of BEIS, to fund the connection of the E.ON biomass plant to supply heat to the Sheffield District Energy Network.

1.2 An opportunity has arisen to obtain funding (a mixture of grant and loan) to support the expansion of the E.ON owned district energy network in the Lower Don Valley to make a connection to the Sheffield City Council district energy network (DEN). This project will:

* Require no direct capital or revenue funding from SCC but will require SCC to be the recipient of grant funding and then pass on grant the funds to E.ON on reciprocal terms.
* As phase 1: Deliver a connection between the E.ON district energy network and the SCC DEN, providing additional low cost, low carbon heat to the SCC DEN providing resilience and opportunities to expand the SCC DEN.
* As phase 2: Deliver connections in the E.ON network to the Northern General Hospital and a BT datacentre.
* Support the city’s regional development growth plan to encourage new industry and investment in the region; assisting with low cost, low carbon heat, improving air quality and ensuring Sheffield’s established and potential new investors are competitive in world markets.

1.3 A separate Business Case will be produced for phase 2 of this project during 2017/18. This Report and the associated Business Case focus on phase 1 only.

1.4 Further approvals will be necessary for Phase 1 of the Project and we will go through the correct governance process to do this. There are various agreements associated with Phase 1 and Phase 2, between E.on and SCC/ BEIS and SCC, which have not yet been finalised and for which we will require further authority. This report is only seeking acceptance of the grant funding and to enter into the MoUs (‘grant agreements’).

* N.B. To secure the grant funding for phase 1 from the HNIP pilot, the Memorandums of Understanding have to be signed by 31st March 2017.

2. **HOW DOES THIS DECISION CONTRIBUTE ?**

(Explain how this proposal will contribute to the ambitions within the Corporate Plan and what it will mean for people who live, work, learn in or visit the City. For example, does it increase or reduce inequalities and
2.1 A number of documents on sustainable local growth and development set the context for this project; these include Sheffield’s Economic Masterplan, Sheffield’s Development Framework, the City Centre Masterplan 2008 and specific Sheffield City Council (SCC) spatial planning policies.

2.2 The sustainability policy “Growing sustainably: a bold plan for a sustainable Sheffield”, was approved at Cabinet recently, and makes several references to the importance of district heating and decentralised energy to delivering sustainability in Sheffield. A more extensive decentralised energy infrastructure would assist with flexibility, resilience and future-proofing of energy provision for Sheffield, together with carbon dioxide emissions reductions and a decrease in local atmospheric pollutants.

2.3 The Sheffield Energy and Water Infrastructure Strategy has indicated that there is an opportunity to extend the existing district heating system or expand it to incorporate other decentralised energy sources, establishing a wider network across the city centre. This would be capable of delivering low-carbon heating, cooling and electricity to other areas of the city, including a variety of building types and energy users, both existing and emerging.

3. HAS THERE BEEN ANY CONSULTATION?
(Refer to the Consultation Principles and Involvement Guide. Indicate whether the Council is required to consult on the proposal, and provide details of any consultation activities undertaken and their outcomes.)

3.1 We believe that no consultation is required.

4. RISK ANALYSIS AND IMPLICATIONS OF THE DECISION

4.1 Equality of Opportunity Implications

4.1.1 An expansion and development of the SCC DEN, which this project will facilitate, will support the attraction of industry and commerce to Sheffield, with resultant employment opportunities.

4.1.2 District heating offers opportunities to use low cost, low carbon heat sources, reducing carbon footprints and improving air quality. An expansion of the DEN to include social housing offers an opportunity to tackle fuel poverty, delivering associated health benefits.

4.2 Financial and Commercial Implications
The overall costs and funding of the wider project as a whole are set out below:

4.2.1 Total project (phases 1 and 2)
The total project, delivering all three legs connecting the SCC DEN, Northern General Hospital, and BT datacentre will have a design and build cost of £13,200,000. It will be funded as follows:

- HNIP Grant: £2,231,250 (two grants combined make this amount)
- HNIP Loan: 3,500,000 (38 year term)
- E.ON funding: £7,468,750
- SCC funding: £0

### 4.2.2 Phase 1

At this point the Council is committing only to delivering phase 1 of the project, the connection between the Blackburn Meadows plant and the SCC DEN. For this phase the cost of the project is £5.0m, to be funded as follows:

- HNIP Grant: £2,231,250
- E.ON funding: £2,768,750
- SCC funding: £0

It is the HNIP grant of £2.232m above that is the subject of the MOU to be entered into.

### 4.2.4 SCC will act as the Accountable Body, drawing down the grant from BEIS as funding requests are received from E.ON against agreed milestones.

### 4.2.5 To secure the grant funding, SCC is being asked to sign the Memorandums of Understanding (attached) and note signed by the s.151 officer, no later than 31 March 2017. The grant can then be drawn down against agreed project delivery milestones during financial year 2017/18.

The only costs to SCC will be minor administrative costs in acting as the Accountable Body, drawing down funds from BEIS and passing them on to E.ON against funding requests and agreed project delivery milestones. The agreement with E.ON will be a ‘back to back’ agreement, replicating the terms and conditions of SCC’s MoU with BEIS, so that SCC takes no risk and incurs no liabilities.

### 4.2.6 Additionally, as part of phase 1, the Council will enter into a heat purchase agreement with Eon which will commit the Council to take a minimum of 7500 MWh of heat at a fixed price. It is anticipated that the price of the heat will be at least comparable to the gas back up currently used by Veolia and will create greater capacity of energy to sell on to third party customers of the DEN. This will subject to a separate approval and the Council will not draw down any funding and pass on to Eon until it is satisfied with the terms of the agreement with Eon and the appropriate approval has been given.

### 4.2.7 The costs of administering the Accountable Body role will be covered through a discount on the price of heat purchased.

### 4.2.8 In addition it is anticipated that as part of phase 2 of the project, where BEIS funding will be through a low-interest loan, SCC will apply a small
margin when passing on the loan to E.ON, to cover the costs of acting as the Accountable Body.

Key features of both of the grant Memorandums of Understanding (not exclusive) are summarised as follows:

• The funder has issued two near identical grant MoU documents, one for commercialisation (£417,500) and one for construction (£1,813,750) which covers a period up to the end of March 2018.

• Nothing in the Memorandum is intended to create legally binding relations between SCC and BEIS or between the SCC and Salix except the clauses around Use of Grant Proceeds and State Aid and breach of law which are legally binding on the parties. However, if the project does go live and the grant is required to be drawn down, SCC will at that point need to have in place further SCC approvals and back to back funding agreements with E.on that pass on all funding agreement liabilities identified in the MoU(s) in order to minimise risks to SCC.

• Once the project proceeds and the grants are drawn down then the grants are subject to a range of clawback conditions if the terms and conditions of the funding agreement are not met. Any unspent grant must be returned to the funder.

• “Eligible Costs” for the project are the capitalised costs for commercialisation, design, construction and commissioning as identified in SCC’s Application and Schedule 1 of the MoU(Project Description)

• The project must be compliant with EU State Aid requirements including General Block Exemption Regulations.

• The funding can be only be used for the project and no other purpose.

• The Grant offer shall expire at the end of the Availability Period if funds have not been advanced prior to that date.

• Should the project proceed all procurement arrangements will need to be done in accordance with the MoU/funding agreement and must also be compliant with European Procurement Rules where required.

• The Project Manager will need to read, understand and comply with both of the MoUs and all associated documentation related to this project..

4.3 Legal Implications

4.3.1 The s.31 grant in accordance with the Local Government Act 2003, has been awarded to the Council by the Department for Business, Energy and Industrial Strategy (BEIS) for the Heat Network Investment Project Pilot. The Council has the power to proceed through the General Power
of Competence in Part 1 of Localism Act 2011. It also has the power to deliver the project, to which the grant applies, under s.111 of the Local Government Act 1972.

There are two grant Memorandums of Understanding one for commercialisation (grant amount £417,500) and one for construction (grant amount £1,813,750) totalling £2,231,250.

The Council will act as the Accountable Body for the grant from BEIS. The Council will enter into separate agreements with BEIS, at a later date and will obtain full approvals for this. These agreements will include a grant agreement between The Council and E.on, where the Council will seek to pass on the obligations under the MoU to E.on, in order to minimise the risks to the Council.

The Council will not make funding requests on behalf of E.on unless and until there is approval and agreement to enter into the grant agreement with E.on. Also any related/necessary agreements linked to the project between the Council and E.on will need to be signed and approved before the Council proceeds with the project.

Although these agreements are MoU’s and therefore in the main are not legally binding, should we sign up to these there is an understanding that we will proceed with Project. Should we then not be able to come to an agreement and move forward with the Project there may be some reputational risk to the Council.

The Project Description at Schedule 1 should detail only Phase 1 information, as the grant funding is only being used for this phase. At the moment Section 2 of Schedule 1 mentions Phase 2, this is an Eon project programme of works chart. There is the risk here that BEIS could infer that the references to Phase two elements are part of the Project Description, for which the grants should be used and we would advise that there is no reference to Phase 2 in Schedule 1.

There are repayment and clawback obligations attached to the funding from BEIS, however the Council will pass these on to E.on via a further funding agreement and the Council would not want to proceed with the Project if these terms are not agreed with E.on (these will be subject to further approvals in any event). The repayment obligations are only relevant if the project proceeds and if we make a claim for funding on behalf of E.on. Repayment of any unspent grant is also necessary, if the Eligible Costs of the Project are less than the Projected Costs.

There are a number of Repayment Events set out at clause 13, including (but not exclusive) non-compliance with the obligations of the grant agreement, insolvency, material adverse change to the business or function which would’ve made a difference to the application being accepted, any event or circumstance which BEIS consider would have a material adverse effect and failure to proceed to construction. The consequences of which could be the grant is cancelled, BEIS declare all
or part of the grant immediately due and payable or payable on demand, with or without interest. In the case of a repayment event due to non-construction, only a portion of the Grant, which has not been spent, will be immediately due and payable or payable on demand.

Please note apart from the cancelling of the grant, these events would only apply if we have drawn down and hold the grant for E.on. There will need to be further authority obtained via the leaders scheme of delegation to do this. This report is only to enter into the grant agreement, the Council will not draw down until it has further agreements in place and the authority to enter these.

The Council is providing indemnities against any cost, loss or liabilities (not exclusive) incurred by BEIS, as a result of the Councils or any Investment Vehicles actions or omissions or in respect of the Project. These obligations will be passed on to E.on via the further agreements proposed.

The Council is being asked to sign the Memorandums of Understanding and a form signed by the s.151 officer, no later than 31 March 2017.

The grants may constitute a state aid and therefore the Council will also have to ensure it is state aid law compliant throughout the Project and has sought external legal advice in this regard from Bevan Brittan Solicitors. They have also provided us with advice in respect of complying with our procurement obligations.

Where appropriate procurements under this Agreement will be subject to European Procurement Rules and the Council will need to comply with these. Procurement of the works must also comply with the Council’s own standing orders.

4.4 Other Implications
(Refer to the Executive decision making guidance and provide details of all relevant implications, e.g. HR, property, public health).

4.4.1 None

5. ALTERNATIVE OPTIONS CONSIDERED
(Outline any alternative options which were considered but rejected in the course of developing the proposal.)

5.1 The HNIP funding application (attached to the OBC) provides evidence that in the absence of the HNIP funding, the project would not be viable. The SCC DEN would continue to rely on gas and oil boilers to provide back-up and top-up heat into the network at times of peak demand and during the Energy Recovery Facility (ERF) shut-down periods. The NGH would continue to rely on its own gas-fuelled energy centre and the BT datacentre would be likely to install a gas CHP energy centre.
5.2 The opportunities for carbon savings for all three organisations would be lost and the SCC DEN would remain unable to achieve significant development and expansion.

6. **REASONS FOR RECOMMENDATIONS**

(Explain why this is the preferred option and outline the intended outcomes.)

6.1 The application for grant funding through the HNIP pilot is the only means of attracting the funding necessary to make the connection between the E.ON biomass plant and the SCC DEN viable at this time.

6.2 If the opportunity is not taken to secure the grant funding there may be opportunities to apply for funding if the HNIP is extended, but this cannot be at all certain.

6.3 This is unique opportunity to secure grant funding for a project with significant opportunities for Sheffield, and at minimal risk and cost to the Council. All agreements with E.ON will seek to try to ‘back off’ and ‘flow down’ and risks, obligations and liabilities to E.ON. SCC will only draw down funding from HNIP when requested by E.ON and once agreed milestones have been completed. The risk of any clawback is therefore minimal, but in any case that risk is also backed off to E.ON. SCC’s only costs will be in administering the ‘Accountable Body’ role to pass HNIP funding through to E.ON who will deliver the project.