




Report to:	Sutton Shareholdings Board	Date:	5 February 2019
Report title:	Sutton Decentralised Energy Network Business Performance Update		
Report from:	Mary Morrissey, Chief Executive (Interim)		
Ward/Areas affected:	Borough Wide		
Chair of Committee/Lead Member:	Councillor Sunita Gordon		
Author(s)/Contact Number(s):	Daniel Doris, Regeneration Programme Manager - 0208 770 4854		
Corporate Plan Priorities:	<ul style="list-style-type: none"> • Living well independently • Smarter ways of working 		
Open/Exempt:	Open with the exception of Appendices B and C (Sutton Decentralised Energy Network Risk Register and Budget Variance for Q3 2018/19) which are exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972.		
Signed:		Date:	29 January 2019

1. Summary

- 1.1 This report is presented for noting the update contained in the Sutton Decentralised Energy Network Performance Report and the un-amended Risk Register. The report provides an update on progress with SDEN Phase 2 and seeks delegation of authority to enter into heat supply contracts with Clarion Housing for the Lavenders development, subject to the final business case being concluded satisfactorily.

2. Recommendations

The Sutton Shareholdings Board is recommended to:

- 2.1 Note the performance update contained in the Sutton Decentralised Energy Network Performance Report in Appendix A.
- 2.2 Note the Sutton Decentralised Energy Network Risk Register in exempt Appendix B.
- 2.3 Note the Sutton Decentralised Energy Network Budget Variance for Q3 2018/19 in exempt Appendix C.
- 2.4 Note the Sutton Decentralised Energy Network Limited Annual Accounts for 2017/18 in Appendix D.

- 2.5 Delegate authority to the Shareholder Representative, or their nominee, in consultation with the Chair and Vice Chair of the Sutton Shareholdings Board, to approve the detailed Business Case for the extension to the Lavenders and enter into heat supply contracts with Clarion Housing.

3. Background

- 3.1 Following the Council's decision in July 2014 to establish an Energy Services Company (ESCo), a detailed business model was prepared to demonstrate the commercial viability of the proposed company. The initial business plan was approved by the OSL Sub-Committee (now the Sutton Shareholdings Board) on 4 August 2015, along with the Shareholder Agreement, enabling Sutton Decentralised Energy Network Limited to be established.
- 3.2 Since the approval of the original Business Plan at OSL Sub-Committee (now the Sutton Shareholdings Board) on 22 February 2016, a revised Business Plan has been approved at the Sutton Shareholdings Board on 27 June 2018. This Business Plan updated on progress made on both Phase 1 and Phase 2 of the network. Agreements have been signed with the heat supplier and homes are being built at the Felnex development (New Mill Quarter).
- 3.3 In line with the SDEN Business Plan, approved by the Sutton Shareholdings Board in June 2018, SDEN has been in discussions with Clarion Housing to agree arrangements for SDEN to extend its heat network from the north of the New Mill Quarter (former Felnex) site to the Lavenders development in Hackbridge.
- 3.4 The Lavenders development contains a mix of dwellings which are being developed by Clarion Housing for both rent and private sale. To meet their low carbon planning obligations, Clarion Housing have indicated they would like to connect to SDEN. There are c460 dwellings at the development, and the estimated pipe length from the New Mill Quarter to the Lavenders is 700m. The indicative capital cost for this extension is £1.2m. As per the reserved matters (part b) within SDEN's Shareholders Agreement, any extension with a capital cost of over £1m requires Shareholder Consent prior to SDEN entering into contracts to supply heat.

4. Issues

- 4.1 A detailed Business Case for the scheme is required prior to any decision being made, however SDEN understands from Clarion Housing that they will be required to sign contracts before the end of March 2019. An outline Business Case has been produced, reviewed and approved by the SDEN Finance Director, supported by financial consultants 31ten. A detailed Business Case is currently being produced, however the decision to enter into contracts is required before the next Sutton Shareholdings Board. Therefore it is recommended that authority is delegated to the Shareholder representative, or their nominee, in consultation with the Chair and Vice Chair of the Sutton Shareholdings Board, to approve the detailed Business Case for the extension to the Lavenders and enter into heat supply contracts with Clarion Housing.

Risk Register



4.2 The Risk Register is attached at Appendix B.

5. Options Considered

Performance Update

5.1 The performance update is attached at Appendix A – Sutton Decentralised Energy Network Performance Report dated October 2018 to December 2018.

6. Impacts and Implications

Financial

- 6.1 In July 2013, the London Borough of Sutton's Strategy and Resources Committee (S&R) approved the Conceptual Business Case for the development of a district heating network in Sutton, with debt funding of £4.5m.
- 6.2 A detailed Financial Model for the Phase 1 Scheme was presented to the Housing, Economy and Business committee in March 2015. This demonstrated a positive cash flow of £1.54m from delivery of the scheme.
- 6.3 The Financial Model has been revised to take account of the latest information on likely costs and revenues. As a result of the revisions the model shows a revised loan requirement of £2.6m and an improved net positive cash flow on core assumptions of £1.64m. A review of the revised model by KPMG has taken place and no material issues were raised.
- 6.4 A financial monitoring report for Q3 2018/19 has been prepared and is attached in exempt Appendix C.
- 6.5 The summary annual accounts for 2017/18 are attached as Appendix D. These were submitted to Companies House on 2 January 2019, making this the first opportunity to present these to the Sutton Shareholdings Board.
- 6.6 The detailed Business Case for the connection to the Lavenders requires further detailed inputs, which are currently being developed. The initial financial modeling within the outline Business Case has a base case Internal Rate of Return (IRR) of 11.76% and cumulative earnings before tax of £1.84m. The outline Business Case has been reviewed and approved by the SDEN Finance Director and reviewed by finance consultants 31ten. 31ten's review found no significant issues with the financial model, and concluded that the scheme as modelled was robust. As stated above, further work is required to confirm the financial metrics, but based upon the outline Business Case the extension to the Lavenders is commercially viable.

Legal

6.7 SDEN is a subsidiary company of Opportunity Sutton. The shareholder agreement between SDEN and its parent company governs the relationship between the two companies and in



schedule 1 there is a list of reserved matters either falling under a Part A (Corporate Matters) or Part B (Operational Matters). As stated above in the report with regards the Lavenders, the indicative capital cost for this extension is £1.2m. As per the reserved matters in Part B (reserved matter 7) within SDEN’s Shareholder Agreement, any extension with a capital cost of over £1m requires Shareholder Consent prior to SDEN entering into contracts to supply heat. This would require shareholder approval from Opportunity Sutton. However, it was intended that SDEN would also be bound to certain reserved matters being subject to the approval of the SSB by virtue of the reserved matters identified in schedule 1 of the shareholder agreement between the Council and Opportunity Sutton. The recommendation with regards the Lavenders is one such decision. Unfortunately, the latter shareholder agreement has not been amended to incorporate SDEN, though this document clearly states it is the intention.

- 6.8 Notwithstanding this, the effect of the governance arrangements between the Council and Opportunity Sutton is intended to cover the subsidiaries where decisions affect the shareholder’s rights. Therefore because of the nature of the matter to be approved in recommendation 2.5, it is advisable that the SSB should treat this as a reserved matter that requires its approval and make a decision with regards recommendation 2.5. Under the new governance structure relating to the SSB it is open to the SSB to delegate to the shareholder representative (or their nominee) in consultation with the Chair and Vice Chair of the SSB as recommended above.
- 6.9 For the purpose of this report, save for the legal implication in paragraph 6.7 above there are no other legal implications as the rest of the report is to provide an update to the shareholder as to the risk register and company performance.

7. Appendices and Background Documents

Appendix letter	Title
A	Sutton Decentralised Energy Network Limited Performance Report
B	Sutton Decentralised Energy Network Limited Risk Register (<i>exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972</i>)
C	Sutton Decentralised Energy Network Budget Variance Q3 2018/19 (<i>exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972</i>)
D	Sutton Decentralised Energy Network Limited Annual Accounts 2017/18

Background documents
Sutton Decentralised Energy Network Limited Annual Accounts 2017/18 - FULL

Audit Trail		
Version	Final	28 January 2019
Consultation with other officers		
Finance	Yes	Lyndsey Gamble
Legal	Yes	Fabiola Hickson
Equality Impact Assessment required?	No	N/A

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