

CABINET

YPO Gas Contract

11th November 2008.

Report of Head of Property Services

| PURPOSE OF REPORT | | | |
|---|-------------------------------------|------------------|------------------------------|
| To consider the procurement of a new Gas contract for a four-year period up to and including 31 st May 2013. | | | |
| Key Decision | <input checked="" type="checkbox"/> | Non-Key Decision | Referral from Cabinet Member |
| Date Included in Forward Plan | | | |
| This report is public | | | |

RECOMMENDATIONS OF COUNCILLOR ARCHER

That the Cabinet accept the recommendation, to move towards a flexible method of purchasing gas energy through the Yorkshire Purchasing Organisation (YPO). The YPO will buy the Council's Gas requirements over several transactions from 1st June 2009 to 31st May 2013.

1.0 Introduction

- 1.1 The Council is a member of the Yorkshire Purchasing Organisation (YPO), a consortium of local authorities from throughout the north of England, which specialises in the procurement of energy and other consumables for local authorities.
- 1.2 The existing four-year Gas supply Contract EN48GS/096 obtained through the YPO expires on the 31st May 2009. The contract accounts for £169,100 of the Council's total gas budget of £395,500. The remaining £226,400 covers a variety of properties including St Leonard's House and Sheltered Housing units, which are currently subject to individual supply agreements. The new Gas Framework offered by the YPO will commence on the 1st June 2009 and will be for a four-year period up to and including 31st May 2013.

2.0 Proposal Details

- 2.1 The YPO recently sought a tender to establish the fixed cost elements (transportation/risk management - not the gas at this stage) from suppliers. Full details can be found on page 1 of the YPO's Confidential Report to Members, Appendix 1. The supplier E.ON Energy proved to be the most economical at the tender stage; details can be found on page 1 of the tender summary Appendix 2.

- 2.2 The tender provides two options for the future purchase gas, based on a comparison of Fixed and Flexible rates.

3.0 Details of Consultation

- 3.1 There has been no formal consultation on this matter by the Council.
- 3.2 The YPO have however consulted its Clients and provided a confidential Report to Members of the Consortium on the mini-tender under Framework 000145 – the Supply of Gas, Appendix 1.

4.0 Options and Options Analysis

- 4.1 Option 1 (Fixed Rate) – This option would result in no change, with the Council continuing to acquire gas under the same sort of contract as now. The YPO will buy the Council's total Gas requirement on one day, when the market conditions are favourable for the period 1st June 2009 to 31st May 2010. Each year thereafter, the same process would be followed to the end of the contract in 2013. The Council will shortly receive from the YPO a cost schedule showing the fixed charges for both options in both pence per kWh and per therm.

Within the recent tender for fixed cost elements it emerged that British Gas and Corona Energy impose certain restrictions. Both will impose additional costs for late payment of invoices and will adjust the contract prices in the event of a shortfall in gas usage. Corona did not quote for all Authorities.

E.ON Energy offer fixed costs with no penalties for late payment and do not require an estimate of usage for the term of the contract. Full details can be found on Page 8 of the main Confidential Report to Members Appendix 1.

Due to the volatility of the market and strong bullish trends there are risks associated with option 1. For example the Council are currently fixed until 31st May 2009 at 78 pence per therm. The wholesale market at 15th October gas was trading at 70.4 pence per unit. Conversely should North Sea production reduce further and if winter weather conditions are colder than usual the market may rise again.

- 4.2 Option 2 (Flexible Rate) - Move to a flexible purchasing option. The YPO will buy the Council's Gas requirements over several transactions. Within this option the Council will still know the Gas price for the full 12 months.

This option will allow the Council to purchase flexibly within the contract period in 5,000 therm clips. The Council can trade live market prices; settlement prices, day ahead and month-ahead index prices, with all purchases made before the 24th of Month i.e. before the month of delivery. For example for August, purchases must be made on or before the 24th of July.

E.ON Energy submitted their General Terms and Conditions of Supply and agreed to give the YPO the ability to do everything outlined in the original tender guidance documents, which were forwarded to all prospective bidders prior to the Tender, these included,

- The ability to fix all non-energy costs prior to contract start up.
- The ability to fix all volume prior to the start of this contract year.
- The ability to purchase in multiple quantities to fulfil the total volume requirement as appropriate.

An important part of the E.ON Energy offer is that they would not impose cash out (take or pay) and therefore under any Contract with E.ON Energy there is absolutely no pressure on members to accurately nominate any likely consumption values for any contract year.

Acceptances for this option should be logged with YPO by Friday 28th November 2008. Any received after that date will not have the opportunity to move to a flexible option and will have to remain on a fixed profile until the next anniversary which will be 1st June 2010.

There are risks associated with purchasing gas on a flexible basis. If for example gas prices increase further and the YPO have not locked onto a fixed rate period the council could be paying more for their gas for a period. For example on 1st June 2007 the council locked on at 63 pence per therm for a twelve month period. Wholesale prices continued to rise throughout the year. As at 1st June 2008 the Council locked on at 78 pence per therm for a twelve month period. Wholesale prices now seem to be falling. As at the 15th October 2008 gas prices were trading at 70.4 pence per therm.

- 4.3 Option 3 do nothing - The existing four-year Gas supply Contract EN48GS/096 with the (YPO) expires on the 31st May 2009. Should the Council chose not to purchase gas on a fixed or flexible basis then the rates charged by the current gas supplier (npower) will go variable until a contract is sought. We are advised by the YPO that the current fixed rate could double under the variable option. Within such a volatile market it is uncertain whether wholesale prices will increase or decrease

5.0 Officer Preferred Option

- 5.1 Option 2 is the preferred option at this stage. It would be to permit the YPO to purchase Gas on a flexible basis from June 1st 2009 to 31st May 2013 with the supplier E.ON Energy
- 5.2 The YPO are hopeful that when the heating season is over, prices should reduce which will put the Council in a position to take advantage of the rates.
- 5.3 The YPO have requested that submissions be logged with them by Friday 28th November 2008. After this date we will not have the opportunity to move to a flexible option and will remain on a fixed option until 1st June 2010.
- 5.4 The OGC Transforming Government project cites that organisations must use a Contract with the ability to fix volumes over a series of purchases in Wholesale traded Gas markets.

5.5 Management of the arrangements proposed under the option can be met from within existing staff resources.

6.0 Conclusion

6.1 Based on the information provided by the YPO the benefits of moving to a flexible option from 1st June 2009 are;

- Price certainty for the full twelve months in advance of the Contract start.
- Reduction of risk.
- Lower fixed cost element.
- Follows the OGC Transforming Government guidelines.
- E.ON Energy do not impose any reconciliation charges on Local Authorities

RELATIONSHIP TO POLICY FRAMEWORK

The Council's Corporate Plan includes action to support sustainable communities and action on climate change. This report has links to that policy

CONCLUSION OF IMPACT ASSESSMENT

(including Diversity, Human Rights, Community Safety, Sustainability and Rural Proofing)

There are no direct links identified within this report as the report relates to the consumption of natural gas. However the preferred option for the new gas purchase contract would allow for the Council to reduce its consumption of gas should the Council's buildings be heated in a more sustainable manner.

FINANCIAL IMPLICATIONS

Of the £396k currently budgeted for gas in 0809 £169k currently falls under the existing contract which will be subject to a revision during the budget process to reflect the current climate, usage and appropriate inflation rates. For comparison, outturn for gas for 0708 for areas relating to the contract was £206k. As the existing tariff is expiring in May 2009, the current costs are likely to increase substantially if no action is taken.

The energy prices have been and remain extremely volatile, and the flexible option for gas purchase appears to provide the option of least risk to the Council. As a member of the Lancashire Procurement Hub, we are currently seeking its officers' views on the proposed arrangements and market conditions and will report any outcome verbally to the meeting

As it is not possible to quantify detailed costings, it is essential that Property Services liaise with Finance to keep them updated with progress as it occurs. Whilst it is anticipated that this option will hopefully prove favourable, due to the current economic climate there are potentially significant risks for any of the options contained within this report.

DEPUTY SECTION 151 OFFICER'S COMMENTS

Given the current economic climate, it is clear that all of the contract options carry a financial risk. The proposed arrangements should provide the Council with the flexibility to manage market risks; it is essential that this is backed up by a system of robust monitoring and review.

LEGAL IMPLICATIONS

Legal services would be consulted on the detail of the contracts pursued through the YPO.

MONITORING OFFICER'S COMMENTS

The Monitoring Officer has been consulted and has no further comments.

BACKGROUND PAPERS

None other than included as appendices to this report.

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