



**Cabinet**  
22 May 2023

**Report from the Corporate Director  
of Finance and Resources**

**Authority to Tender Contract to Design, Build, Operate and  
Maintain the South Kilburn District Heat Network**

<b>Wards Affected:</b>	Kilburn
<b>Key or Non-Key Decision:</b>	Key
<b>Open or Part/Fully Exempt:</b> (If exempt, please highlight relevant paragraph of Part 1, Schedule 12A of 1972 Local Government Act)	Open
<b>No. of Appendices:</b>	None
<b>Background Papers:</b>	None
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**1.0 Purpose of the Report**

- 1.1 This report concerns the district heat network in South Kilburn which will provide low carbon heat to the South Kilburn regeneration programme. This report requests approval to invite tenders in respect of a contract for a Design, Build, Operate and Maintain contractor, through a competitive dialogue procedure, as required by Contract Standing Orders 88 and 89.
- 1.2 This report highlights the offer of £4.7m of grant from the Green Heat Network Fund (GHNF) towards the costs of constructing the district heat network and

£0.45m towards the council's costs to procure the network including internal and external costs.

## **2.0 Recommendation(s)**

That Cabinet:

- 2.1 Approves inviting tenders to Design, Build, Operate and Maintain the South Kilburn Heat Network on the basis of the pre - tender considerations set out in paragraph 3.11 of the report.
- 2.2 Approves Officers evaluating the tenders referred to in 2.1 above on the basis of the evaluation criteria set out in paragraph 3.11 of the report.
- 2.3 Notes the award of a grant of £4.7m from the Green Heat Network Fund is to be applied towards the costs of constructing the district heat network and £0.45m towards the council's costs to procure the network.
- 2.4 Notes that the project utilises S106 funds specifically allocated as set out in paragraph 5.4.
- 2.5 Approves the allocation of an estimated £5.3m from prudential borrowing, to fund the remainder of the scheme.

## **3.0 Detail**

- 3.1 The South Kilburn District Heat Network will be a network of pipes feeding heat to the buildings in South Kilburn.
- 3.2 The use of a district heat network is in-line with GLA policy and Brent's Local Plan. For South Kilburn, the heat network aims to initially provide low carbon heat but ultimately to provide zero carbon heat to developments in South Kilburn which form part of the South Kilburn Regeneration Programme along with additional connections where appropriate and practicable.
- 3.3 The Critical Success Factors for this project are:
  - Ensures affordable low carbon heat to all residents in South Kilburn buildings which are connected to the network;
  - Provides low carbon heat to developments in South Kilburn in order to help enable them to comply with the energy requirements of the London Plan;
  - Provides a service which residents believe is satisfactory and value for money;
  - Provides CO<sub>2</sub> savings contributing to the Council's aspiration to be net zero carbon by 2030;
  - Delivers an employment and training programme to enable local residents to work on the installation and management of the project.

- 3.4 Having sought and reviewed external consultancy advice on a range of delivery options, Officers' preferred way to deliver the area wide network of pipes supplying the buildings within the South Kilburn Regeneration Programme (the "Estate") with heat and hot water is that Brent Council will directly contract and client a single contractor who will design, build, operate and maintain the generating system and its distribution pipes to connected buildings on the Estate.
- 3.5 By the Council managing the system, it will be able to control the system including setting the heat tariff for the network. Brent will bill the residents in Brent Housing managed buildings based on consumption and supply heat in bulk to the buildings that are managed by others such as the Housing Associations, building management organisations, schools, affordable workspaces, retail and medical facilities. Users, including residents, will have full control over their systems in terms of time and temperature control.
- 3.6 One of the Critical Success Factors is to provide affordable heat to residents in South Kilburn. This will be achieved as Brent will manage the heat tariff. One of the key components of the heat tariff is the cost of fuel. As Brent will manage the system, Brent will procure the fuel for the network through its favourably priced public sector buying process. This process has resulted in competitive prices throughout the current volatile energy markets.
- 3.7 The preferred technology solution is to use air source heat pumps either with gas boilers to provide back-up or electric boilers. These are coupled with thermal stores to manage peak heat demands. The final technological solution will emerge through the proposed competitive dialogue process for procuring a Design, Build, Operate and Maintain Contractor.
- 3.8 Officers have reviewed the procurement and delivery options for a heat network in the context of the project's critical success factors and the project risks. Officers have also considered commercial implications to ensure that the network will offer best value to the council and the network customers. The proposal to procure a Design, Build, Operate and Maintain Contractor ensures that the contractor is responsible for the quality of the construction and that the contractor will ensure that the network will operate efficiently. This type of contract also offers the opportunity for the local community to engage with the contractor to ensure that their priorities can be met.
- 3.9 Officers have undertaken soft market engagement to understand the market position with regard to procuring a heat network. This engagement considered the market position with regard to the proposed procurement through Competitive Dialogue, the appetite of the market for this project, contract length, mitigation for the volatility of the construction market and other project specific considerations.
- 3.10 The responses to the soft market engagement were generally positive and contractors were keen to engage in the project. Ten contractors participated in

focused sessions supporting the Council to ensure procurement offers the most favourable opportunities for the market whilst ensuring best value and good quality for the Council. In summary:

- All contractors were engaged and interested in the potential for the South Kilburn Heat Network.
- Overall, the response to the quality/price split was quite balanced, but with a slight favouring towards a higher score for quality.
- Overall, the respondents welcomed the use of Competitive Dialogue but noted the requirement to be clear on what was open for Dialogue.
- Overall, the respondents agreed that a term of 15 years was appropriate as long as this included provision for extending the contract.
- Respondents highlighted the risks of the heat demand and distribution in the buildings not being optimised with the design of the heat network and discussed solutions to mitigate for that risk.
- Several other risks were highlighted based on contractor experience. In particular, the requirements of Highways need to be clear as part of the procurement documents to avoid later delays and price increases and provision of information by the council on ground risk.
- Respondents highlighted some likely changes to the law which could impact any heat network however, the decarbonisation of the network is a key mitigation. A number of respondents highlighted that the use of gas boilers is a risk due to changes in legislation and they proposed alternatives.
- Planning risk was also highlighted which can be mitigated by applying for planning permission prior to signing contracts.

3.11 In accordance with Contract Standing Orders 88 and 89, pre-tender considerations have been set out below for the approval of the Cabinet.

<b>Ref.</b>	<b>Requirement</b>	<b>Response</b>	
(i)	The nature of the works and services.	Design, build, operate and maintain the South Kilburn District Heat Network.	
(ii)	The estimated value.	Works £17.5m (15 years initial term) £19m (25 years extended term) Services £9m (15 years initial term) £17m (25 years extended term)	
(iii)	The contract term.	Initial period of 15 years with a potential to extend for up to an additional 10 years.	
(iv)	The tender procedure to be adopted.	The Competitive Dialogue Procedure (CD). The grounds for use of CD are set out the Legal Implications section of this report.	
v)	The procurement timetable.	Indicative dates are:	
		Adverts placed	12/06/2023

Ref.	Requirement	Response	
		Selection Questionnaire returned	21/07/2023
		Shortlist drawn up in accordance with the Council's approved criteria	04/08/2023
		Invite to Participate in Dialogue	18/08/2023
		Invitation to Submit Final Tenders	10/03/2024
		Deadline for tender submissions	30/03/2024
		Panel evaluation	April 2024
		Contract decision	May 2024
		Report recommending Contract award circulated internally for comment	May 2024
		Cabinet approval	June 2024
		A minimum 10 calendar day standstill period – notification issued to all tenderers and additional debriefing of unsuccessful tenderers	10 day call in
		Contract Mobilisation	July 2024
		Contract start date	August 2024
(vi)	The evaluation criteria and process.	1. At selection stage shortlists are to be drawn up in accordance with the Council's Contract Procurement and Management Guidelines by the use of a selection questionnaire to identify organisations meeting the Council's financial standing requirements, technical capacity and technical expertise. The selection stage will include scoring to ensure the quality of the bidders to be taken forward for dialogue.	

Ref.	Requirement	Response
		<p>2. At tender evaluation stage, the panel will evaluate the tenders against the following criteria:</p> <ul style="list-style-type: none"> <li>• <i>Quality - 50%</i></li> <li>• <i>Price - 35%</i></li> <li>• <i>Social Value - 10%</i></li> <li>• <i>Commercial/Risk* - 5%</i></li> </ul> <p>These criteria support the goal of enhanced quality of service provision, given the long term nature of the contract and the services to residents, at a competitive price.</p> <p>*The full Tier 1 criteria for Commercial and Risk is: acceptability of the contractual and risk position based on bidder commentary on and/or mark-up of the Contract, including both the Conditions of Contract and the Schedules.</p>
(vii)	Any business risks associated with entering the contract.	The business risks considered to be associated with entering into the proposed contract are included in paragraph 3.13 below. Financial Services and Legal Services have been consulted concerning this contract and have identified the risks associated with entering into this contract set out in sections 5.0 and 6.0 of the report.
(viii)	The Council's Best Value duties.	The council will undertake a competitive tender process to ensure best value.
(ix)	Consideration of Public Services (Social Value) Act 2012	10% of the evaluation is included for Social Value
(x)	Any staffing implications, including TUPE and pensions.	See section 9.0 below.
(xi)	The relevant financial, legal and other considerations.	See sections 4.0, 6.0 and 9.0 below.
(xii)	Sustainability	This project supports the Council's Climate & Ecological Emergency Strategy (2021-2030) in reducing carbon emissions for a large number of dwellings in South Kilburn. Procurement will take

Ref.	Requirement	Response
		into account specific objectives in-line with the Council's Sustainable Procurement policies reducing carbon both in operation and in construction and minimising the generation of other harmful gases and impacts.
(xiii)	Key Performance Indicators / Outcomes	Appropriate Key Performance Indicators / Outcomes will be included in the contract.
(xiv)	London Living Wage	The Contract will require the payment of the London Living Wage.
(xv)	Contract Management	A contract manager will be appointed and appropriate contract management provisions will be included in the contract.

3.12 Cabinet is asked to support these proposals as set out in the recommendations and in accordance with Standing Order 89.

3.13 The key risks associated with this district heating network procurement are described in the table below.

Risk	Likelihood	Severity	Rationale and Mitigation
Little competition during procurement because no bidders or too few respond - cost higher and potentially project delays	Medium	High	<ul style="list-style-type: none"> <li>Proposing a structure based on detailed analysis of the project financial performance and low carbon technical concept design.</li> <li>Presenting the project to the market with clear risk allocation and clear decision-making within Brent. There are a number of contractors whose business model is to deliver this project delivery approach and strategy.</li> <li>The proposed one stage Competitive Dialogue procedure is favoured by the market.</li> </ul>

<b>Risk</b>	<b>Likelihood</b>	<b>Severity</b>	<b>Rationale and Mitigation</b>
Significant increase in gas/electricity prices resulting in negative impact on Opex	High	High	<ul style="list-style-type: none"> <li>Considering different purchasing strategies for gas, fixed price has cushioned the network over the winter 2021/22 price hikes. Liaising closely with energy broker. Cost passed on appropriately to customers.</li> </ul>
Failure to agree metering, billing, tariff setting across development	Medium	Medium	<ul style="list-style-type: none"> <li>Implement and continue to develop and refine MBT policy throughout project development.</li> </ul>
Brent owned district heating network fails to make a surplus and accumulates debt due to a misalignment between assumptions and critical success factors behind the recommendation and business as usual.	Low	High	<ul style="list-style-type: none"> <li>A robust forecasting system and decision-making escalation process will be put in place to foresight difficulties and to timely address them.</li> <li>A tariff review will be done every six months instead of annually.</li> </ul>
Certainty of costs: cost impact of technical risks; un/under-estimated capital costs; changes in capital cost due to events including inflation; market response to procurement puts project viability at risk	High	High	<ul style="list-style-type: none"> <li>Quality commercial and technical advice;</li> <li>Customer sales pricing reflect change in costs - no promises until certainty</li> <li>Cost management within contracts can reduce risk</li> <li>Soft market testing</li> </ul>



## 4.0 Alternative Options Considered

- 4.1 Alternative heating strategies have been considered. The alternative to the use of a heat network is that each building within South Kilburn will have its own communal system in-line with the GLA policy and the low heat demands of new buildings.
- 4.2 These systems would have been procured and managed by private organisations which would likely result in higher costs to Brent's residents. In addition, each building would require roof mounted systems, which increases construction costs, to facilitate the extra weight on the roof, increased internal plant space which would result in a reduction in the dwelling provision and the over provision of equipment.
- 4.3 Heat networks offer significant economies of scale by centralising heating plant and reducing the overall equipment required in an area. The proposed strategy also ensures that buildings connected to the network are supplied with low carbon heat with a strategy to achieve zero carbon in-line with the Council's Climate & Ecological Emergency Strategy (2021-2030).

## 5.0 Financial Implications

- 5.1 The estimated value of the Capital Expenditure works is £17.5m in relation to the 15-year lifespan of the network initially planned. This increases to £19m if the lifespan of the network is extended to 25 years. The cost of operating and providing the heat network services is estimated at £9m under a 15-year lifespan, or £17m if the lifespan is extended to 25 years.
- 5.2 It is anticipated that the cost of this contract for the initial term will be funded from the following sources:

Source	Amount
S106 – specific amounts collected against new developments in South Kilburn	£7.5m
Green Heat Network Fund Grant	£4.7m
Prudential Borrowing	£5.3m

- 5.3 The Green Heat Network fund is providing a further £0.45m of funding towards the procurement costs. This is in addition to the £4.7m grant funding towards the development of the heat network.
- 5.4 The South Kilburn District Heat Network project utilises S106 funds specifically allocated. The amount collected to date is ~£4m. All new developments in the Estate are required to contribute towards the network. The current contribution is £4,000 per dwelling. This is based on the offset cost by not needing to install air source heat pumps in each building. The total expected in relation to this procurement is £7.5m over the next 5-10 years dependent on the South Kilburn construction programme.

5.5 Costs of the project will be met from income generated through charging for heat in accordance with the Heat Metering and Billing Regulations and the Heat Trust Guidelines or subsequent regulatory requirements.

## **6.0 Legal Implications**

6.1 As detailed in paragraphs 3.4 and 3.5, Officers recommend a Council owned, managed and delivered district heat network having sought external legal and consultant advice and having considered a range of alternative options.

6.2 In establishing a district heat network, the Council can rely on powers under section 111 (1) of the Local Government Act 1972 given that the supply of energy to Council tenants, RTB leaseholders, schools and the medical centre are reasonably incidental to the Council's housing function and duties, its LEA duties and its public health and shared social and health care duties.

6.3 Where the Council is relying on its subsidiary powers under section 111 (1) of the Local Government Act 1972 to authorise the provision of a service to facilitate the discharge of a specific function, the Council is permitted to charge for services and supplies provided by the district heat network under section 93(1) of the Local Government Act 2003 ("2003 Act") for that function related service by virtue of section 93(7)(a) of the 2003 Act. Section 93 of the 2003 Act only permits a local authority to recover the cost of supply but does not permit the generation of additional income. The local authority does however have some discretion in assessing what is covered by cost recovery and this may include the costs for provision of replacement equipment.

6.4 Whilst the Council will own the assets, it would intend procuring and managing a single contractor that will design, build, operate and maintain the district heat network and therefore seeks authority to procure such contractor as set out in Recommendations 2.1 and 2.2. The estimated value of such contract is such that it will be above the Public Procurement Regulations 2015 (the "PCR 2015") threshold. Section (iv) of the table at paragraph 3.11 indicates an intention to use a Competitive Dialogue Procedure to procure the contractor. Such procedure is permitted in accordance with Regulation 26 (4)(a)(iii) of the PCR 2015 on the basis that "the contract cannot be awarded without prior negotiation because of specific circumstances related to the nature, the complexity or the legal and financial make-up or because of risks attaching to them". The services in scope of the contract are sufficiently technically, commercially (in terms of cost and risk allocation) and legally complex to justify its use.

6.5 The procurement would be subject to the Council's own Standing Orders and Financial Regulations in respect of High Value Contracts given the estimated value of the procurement. For High Value Contracts, Cabinet approval must be sought to agree the pre-tender considerations and inviting of tenders.

6.6 As set out in Recommendation 2.3, Officers have been awarded funding from the Green Heat Network Fund. The Corporate Director or Director has delegated authority pursuant to paragraph 9.5 and 9.7 of Part 3 of the Constitution and Financial Regulation 8.2.2 of Part 2 of the Constitution to enter into such grant funding arrangements. Once the Council has entered into the grant agreement, it must act in accordance with its grant conditions.

## **7.0 Equality Implications**

7.1 Pursuant to s149 Equality Act 2010 (the “Public Sector Equality Duty”), the Council must, in the exercise of its functions, have due regard to the need to:

- (a) eliminate discrimination, harassment and victimisation and other conduct prohibited under the Act
- (b) advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it; and
- (c) foster good relations between persons who share a relevant protected characteristic and persons who do not share it,

7.2 The Public Sector Equality Duty covers the following nine protected characteristics: age, disability, marriage and civil partnership, gender reassignment, pregnancy and maternity, race, religion or belief, sex and sexual orientation.

7.3 Having due regard involves the need to enquire into whether and how a proposed decision disproportionately affects people with a protected characteristic and the need to consider taking steps to meet the needs of persons who share a protected characteristic that are different from the needs of persons who do not share it. This includes removing or minimising disadvantages suffered by persons who share a protected characteristic that are connected to that characteristic.

7.4 There is no prescribed manner in which the council must exercise its public sector equality duty but having an adequate evidence base for its decision is necessary.

7.5 This project has potential equality impact implications in terms of ability of residents to pay for heat and to ensure that dwellings are affordable to heat.

7.6 The Council’s Metering and Billing policy reviewed these equality implications and noted that the proposal to use credit billing managed by the Council ensured that any equality implications are mitigated within that process.

7.7 The procurement of the district heat network itself has no adverse equality implications.

## **8.0 Consultation with Ward Members and Stakeholders**

8.1 Engagement with the management of existing blocks and developers delivering blocks in the masterplan is ongoing.

8.2 Consultation with Kilburn Ward Councillors is also ongoing.

## **9.0 Human Resources/Property Implications (if appropriate)**

9.1 The proposal is to manage the network in house. This will require additional staff including a contract manager and officer to support residents. This will be funded through the heat income from the project. Any additional resource would result in additional costs which could increase the heat tariff.

9.2 For blocks managed by Brent, there is an aspiration that the Design, Build, Operate and Maintain contractor would take over the maintenance responsibility of automated meter readings, the heat interface units (HIUs) within dwellings and the heating distribution within the blocks from Brent Housing Property Maintenance. Brent Property will also have legal agreement for the Energy Centre (either license or lease) and the DBOM will maintain and operate the centralised heating generating plant/s.

## **10.0 Public Services (Social Value) Act 2012**

10.1 The Council is under duty pursuant to the Public Services (Social Value) Act 2012 (“the Social Value Act”) to consider how services being procured might improve the economic, social and environmental well-being of its area; how, in conducting the procurement process, the Council might act with a view to securing that improvement; and whether the Council should undertake consultation. This duty does not strictly apply to the proposed contract as it is not a services contract. Nevertheless, Officers have had regard to considerations contained in the Social Value Act in relation to the procurement.

10.2 Officers recommend that social value comprises 10% of the evaluation score as detailed in section (vi) of the table at paragraph 3.11.

**Report sign off:**

***Minesh Patel***

Corporate Director, Finance and Resources