

ECONOMY, ENERGY AND FAIR WORK COMMITTEE

PUBLICLY OWNED ENERGY COMPANY INQUIRY

SUBMISSION FROM Phil Brennan – Association for Public Service Excellence

Scottish Publicly Owned Energy Company (POEC)

1. APSE and APSE Energy

The Association for Public Service Excellence (APSE) represents council officers and members involved in the management and provision of quality public services. APSE's mission statement positions the organisation as "networking organisation which consults, develops, promotes and advises on best practice in the delivery of public services". APSE is currently working with almost 300 authorities within the United Kingdom. APSE members are local authorities, and a small number of other public service providers, from across the UK and we run the largest public sector performance management and benchmarking model in the UK and probably Europe, Performance Networks.

APSE Energy is part of the APSE family and is a collaboration of local authorities with a vision of the 'municipalisation of energy services', to increase the level of influence that local authorities have over the energy agenda in their locality. APSE Energy keeps its members up to date with developments across the sector, has a role as advocate for local government across the energy agenda and facilitates knowledge and experience sharing within the sector. As an organisation which is owned by our local authority membership, we can provide a unique perspective across the sector.

APSE Energy is pleased to be able to respond to the call for views by the Scottish Parliament in relation to the proposal for the Scottish Government to establish its own publicly owned energy company(POEC).

We are ideally placed to respond to this call, bearing in mind that it has extensive experience of publicly owned energy services company (ESCO) work and has also advised a number of local authorities in Scotland on this very issue.

APSE Energy provides a significant amount of consultancy support to local government. It is currently working on a number of ESCO related projects. It has advised Highlands Council, Aberdeen Council and Orkney Council in Scotland; it is advising Swansea Council at present in Wales; and is advising 14 authorities in the Solent region of England – all about either establishing a fully licensed energy company or some form of white label arrangements.

APSE Energy is responding to this call for evidence on behalf of its membership.

2. Our View of What Works

Introduction

APSE Energy has provided advice to clients, prepared a number of guides and ran numerous events and seminars on the subject of energy services companies including our detailed guide 'Energy Services Companies, White Label Arrangements and Their Role in Local Government,' which was published earlier this year. A copy of this paper is enclosed.

Much of what has been promoted by APSE Energy has been picked up by others and this thinking features in both the Scoping Note by the University of Strathclyde and the Ernst & Young report for the Scottish Government.

Our View of What Works

As the APSE Energy vision indicates, we believe that the only way energy will prosper in public sector hands is at local authority level. A national government company is unlikely to be the answer, as a 'bottom up' approach is required, not a 'top down' approach.

We have undertaken extensive work on what will succeed in this market and the approach that local authorities should take. In short:

- this is a competitive market;
- every company needs a unique selling point;
- the private sector goes for cheapest price, customer service, etc;
- publicly owned companies have to distinguish themselves from these companies and play to their strengths;
- they do this by focussing on their market: the under privileged, the poor, the fuel poor, the vulnerable, those in receipt of welfare benefits, etc;
- local government has far better access to these groups;
- once the ESCO secures them as customers they are unlikely to ever switch away as they want a service provider which they can trust;
- the offer is a constantly discounted price (though not necessarily the cheapest) along with good customer service;
- there are no profits paid to 'fat cats' in the private sector and all surpluses are fed back into public services;
- and a wider role than just energy supply – energy services companies have a much more important role around encouraging the use of less energy and improving energy efficiency, for the wider benefit of the community.

This is a powerful model but one that will not work for Central Government. This is because it does not have the same community links as exist at local level.

Types of Company

Much work has been done on options for energy companies. These can be summarised as:

- fully licensed company;
- white label or white label plus;
- joint venture company with public or private sector;
- licence lite;

- purchasing an existing company.

There are two excellent examples in England of fully licensed companies in Nottingham and Bristol. Both are well planned and organised and are trading successfully. In Scotland, Our Power has a slightly different focus mainly around housing and voids. Licensed companies can definitely work in the right circumstances.

White label arrangements can also work but most local authorities have been disappointed with the deals on offer. White label involves considerable work and little financial reward and if this market is to grow this issue needs to be addressed. The evidence suggests that It is unlikely that a Scottish Government offered white label would be attractive to many local authorities.

Licence lite has been overtaken now and is unlikely to play any significant role in local government in our view. The GLA has been working on this for years and has still not managed to complete the exercise.

Joint ventures are now coming forwards. In Newcastle, the North East Procurement Organisation (NEPO) has commissioned work on how a joint local authority deal might be structured. However to date there are no working examples.

We believe that purchasing an existing company is not the answer as such a company was established with its own business case, purpose, aims and aspirations and particular company constitution. All this would need to be changed if such a company were to be turned into a public venture and it would be easier to start from scratch.

All of these issues are discussed and explained in more detail in the APSE guide referred to above.

So the fully licensed company and the white label plus options are the ones under most scrutiny and are both relevant to this exercise.

Role of the Scottish Government

We believe that the role of the Scottish Government is to facilitate a fairer energy market in Scotland, rather than to intervene in the market itself. There is particular risk for the Government, particularly as it currently has no proper plan of how it is going to do this. As you will understand, making a political commitment is one thing: setting up a fully licensed energy company is quite another.

The Government can undertake this facilitative role quite effectively and easily. It needs to create the circumstances where civic energy companies are created at local level by relevant local authorities. It can oversee the process and provide help and assistance. It can also put in place governance arrangements to ensure that this process is succeeding.

A model that would work would be for the Scottish Government to create an agency to undertake this role. This would have as its members people with experience of what needs to be done and how to do it. It can co-ordinate the process of seeking local authorities to

step up to the plate. We know from our experience that there are a number of local authorities in Scotland that want to do this.

The establishment of the actual energy companies will then be undertaken by a single or groups of local authorities. The provision of help and resources from the Government can be on the basis that surpluses from the operation of the companies is either passed on to customers or used to provide wider energy services which are currently not funded, such as awareness and energy efficiency.

Government Control

As is clear from the last paragraph, we believe that the government's role should be facilitative, providing funding, help and assistance to ensure that the intervention in the market that is sought actually happens, without making that intervention directly itself. That way, the politicians succeed in achieving the outcome, without the risk or extensive resources required.

Should the Scottish Government not agree with that proposition, then there is an alternative, although this is less attractive to local government. Under this route, the Government would set up a holding company and then the local ESCOs are set up as subsidiaries of that holding company.

This is considerably less attractive to local authorities as they will see this as unnecessary governmental control. The Scottish Government wants an the outcome and it should leave the arrangements at local level to be flexible. That way, it will be voluntary if local authorities want to get involved (and not all of them will) and the provision of services at local level might also differ, depending on need and priorities in that area.

Finally, a third possible avenue is to choose a single local authority to act as the Scottish Government's agency and to operate the ESCO on its behalf. Again, this could be by way of some form of subsidiary to the main company which the Scottish Government would own.

Of these options, in our view the facilitative role is by far the most powerful. The Scottish Government only needs to put in place the building blocks and all the main work is undertaken at local authority level. The primary governmental role is to raise awareness and encourage switching to the public sector entity.

3. Why ESCOs are Key

The argument for ESCOs can be summarised as follows:

- the electricity market is broken;
- the Competition and Markets Authority report of 2016 independently confirmed that consumers have been paying too much for their electricity and gas for decades;
- people deeply distrust energy companies, particularly the 'big six';
- there is profiteering at public expense;
- people want more green energy and renewables;
- but they are nervous about switching and wonder if it is worth it;

- there is no emphasis on energy use reduction;
- and there is insufficient emphasis on energy efficiency and its importance.

So in short, something needs to be done. The market is broken and needs a radical overhaul. The big six companies are losing market share but only slowly. The answer is a civic intervention in the market.

Local authorities have a strong covenant with the public. They are trusted. It is public money, with no 'fat cats' involved. If it is non-profit distributing, then public services and the local economy will benefit. This is a powerful message for the average consumer in any area of Scotland.

However local authorities have a further advantage: they are closely linked with the very groups in the population who need the help most i.e. the fuel poor and vulnerable. So they can use all of the various groups that they are involved with to promote the new ESCO. This might include community groups, development trusts, poverty intervention services, benefits services, social housing, housing associations and so on. Finding the customers is key to the long-term success of the ESCO and its not the regular switchers that they want, but members of these vulnerable groups.

A properly planned and created fully licensed ESCO has many advantages, both financial and non-financial:

- the effective addressing of the hugely difficult (and worsening) problem of fuel poverty;
- assisting people to understand energy better and to help them to help themselves to control and manage their bills;
- engagement with the community;
- creation of jobs and growth in the local economy;
- promotion of more renewable energy generation at local level;
- assisting with the demands on the electricity grid by smart controls and better usage.

Financial benefits include surpluses that can be used to pay off the costs of establishing the ESCO and thereafter for investment in wider services, particularly those that cannot be funded in any other way, such as energy awareness.

Local authorities previously ran electricity and gas services across the UK and there is no reason why they cannot be involved in the 21st century. The main problems are raising the finance and risk but both of these can be managed if a fully planned and cautious approach is followed.

4. The Scoping Note

APSE Energy agrees with most of what is included in the Scoping Note. It provides four over-arching objectives for the POEC and each is a valid interest for the Scottish Government.

Paragraph 2.4 confirms that the rationale is to address fuel poverty, provide greater choice for consumers, contribute to economic development and help to deliver wider Government

ambitions on energy. Our point is that the Government does not need to establish its own ESCO to achieve these objectives.

Paragraph 3.4 suggests that in the current market, the successful suppliers are those that can procure energy at lowest prices, have most efficient billing and CRM systems and are best at hedging risk. Current suggestions are that pre-tax margins are around 5%. However, local authority ESCOs do not need to have the cheapest prices, just competitive prices and a very strong link to their customers via the civic brand. Their role, in our view, cannot easily be compared with that of private sector providers.

Paragraph 4.24 recognises that there is likely to be an increasing diversity of approaches across Scotland and “there is a risk that (a Government ESCO) could stifle local innovation if it were too centralising and directive.” This is our point precisely, by engaging with the rich potential of local government, the Scottish Government can achieve its objectives far more easily.

It is also interesting that paragraph 5.2 points out that the report by Ernst & Young to provide the Strategic Outline Case (SOC) for the Scottish Government, “takes the POEC in a particular direction, away from having a more strategic role, and narrows down its purpose to that of an energy supplier.” We would also agree with this point – the real benefit of ESCO’s is that wider role that they can play, which distinguishes them as energy services companies rather than energy supply companies; a role that their profit driven private sector counterparts are simply not interested in.

5. The Strategic Outline Case

As indicated above, the Strategic Outline Case was prepared by Ernst & Young and was published on 29 March 2018.

This ‘presents the case for change for the Scottish Government to establish a publicly owned energy company’.

As might be expected from the authors, this report focusses too heavily on the financial aspects and continually compares the position with private energy companies. Our point is that a public company is a different venture, with different goals and a more compelling unique selling point (USP). As such, whilst we appreciate that it cannot offer prices higher than everyone else (or it will not attract customers easily), it does not need to be the cheapest in the market. Such thinking promotes a ‘race to the bottom’ on prices which risks public money.

A number of options are canvassed in Section 3.2, including at paragraph 9 the provision of a local authority ESCO, over which the Scottish Government would have no direct control. Sadly, this does not find its way into the Executive Summary, clearly indicating that either E & Y did not favour model this or that its brief canvassed against this.

The HM Treasury process means that this Strategic Outline Case is followed by two more stages, namely the Outline Business case and Full Business Case. However, it is important

that these following stages focus on the right options and not the wrong ones and we are not confident of this from the Executive Summary.

6. Specific Questions Asked

The Call for Views asks some specific questions and for the sake of clarity, we list these below. We believe that we have answered these questions and make reference to the comments above:

- What are your general views on the idea of a Scottish publicly owned energy company (POEC)?

This is good idea, depending how it is done.

- What role should it fulfil and how?

It should have the role suggested in the Scoping Note and have a wider purpose than just energy supply. But this has to be at local level.

- What are the key challenges that the POEC should address?

The key challenge is what will work? A top down company owned by central government will never have the reach that comes from a bottom up company owned and operated by a local authority.

- How might a Scottish energy supply company work best to support the growth of local and community projects, and fuel poverty reduction?

If a public company is set up, it can offer competitive prices, good customer service, obtain customers persuaded by the wider benefits and its non-profit distributing nature and invest surplus funds into other beneficial areas. The attraction of the right type of customers will gain traction and the more successful the venture is, the easier it will be to increase energy awareness and promote renewable energy.

- How can the POEC be best designed to align with wider Scottish energy policy objectives, and to avoid potential policy conflicts?

This can be achieved by the Scottish Government facilitating it and not delivering it directly. The liaison with local government is key here.

- Should a new Scottish POEC be more than solely a licensed energy supply company? Should it have a direct role in energy generation?

It is not necessary to be directly involved in energy generation but should promote renewable energy. More beneficial for the ESCO would be to work on public awareness and understanding of energy, reducing energy use and promoting energy efficiency to control bills.

- How might the POEC be designed to promote objectives and functions beyond the retail of gas and electricity (e.g. supporting investment and innovation in new technologies and infrastructure)? What benefits are there to having wider objectives?

This is discussed in the comments above.

- What governance arrangements should a Scottish POEC have? Who should it be accountable to e.g. Parliament?

There are different ways that this could be achieved. If a local authority solution is chosen, then an executive agency of some sort could oversee this. If the Scottish Government is to establish its own wholly owned company then this has to be accountable to the Scottish Parliament.

- Should legislation be required to underpin the creation of a POEC?

This is not necessary. Legal powers already exist for the establishment of civic ESCO's at local authority level.

7. Conclusions

As has no doubt been realised since the initial political commitment was made by the First Minister, ESCO's are a complex and difficult topic to master.

As things currently stand, it will take the Scottish Government until at least 2021 to decide on its path and make its strategy and it will be some years yet before such a company starts trading.

The APSE Energy proposal above could be operational before 2021 and the Scottish Government could be benefitting from the desired outcomes before the end of the current Parliament.

If the Scottish Government does decide to progress its proposals for its own company, in our opinion it will have missed a golden opportunity to put in place better arrangements that are easier, cheaper, provide less risk to the Government and are far more effective.