2017

IWA's Re-energising Wales Project 'Funding Renewable energy Projects in Wales' roundtable

6th June 2017
Eversheds-Sutherland Offices, Cardiff

MAKING
WALES
BETTER

Participants

Auriol Miller, Director, IWA (Chair)
Shea Buckland-Jones, Re-energising Wales Project Coordinator, IWA
Rhea Stevens, Policy, Projects and External Affairs Manager, IWA
Eurfyl ap Gwilym, IWA Board Member
James Thelwell, Investment Officer, GLIL Infrastructure LLP
Professor Calvin Jones, Professor of Economics, Cardiff University Business School
Jennifer Pride, Head of Renewable Energy Team, Welsh Government
Sophie Howe, Future Generations Commissioner for Wales
Mick Brown, Chief Executive Officer, Robert Owen Community Banking Fund
Jeremy Smith, Head of Development Strategy, Innogy
Dan McCallum, Awel Aman Tawe
Jonty Graham, Director and Head of Institutional Capital, Foresight Group
Yvonne Keitch, Senior Accountant, Pension Fund & Treasury Management, Rhondda Cynon Taf County Borough Council
Debbie A Fielder, Pensions Finance Manager, Clwyd Pension Fund
Murray Taylor, JLT Benefits Solutions
Helene Winch, HSBC Global Asset Management
Bruce Davies, Founder and Joint Managing Director, Abundance Investment
Keith Jones, Environmental Advisor, National Trust

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Welcome and introductions

Opening the roundtable discussion, Auriol Miller, Director of the IWA and Chair of the event, noted the objectives of the discussion were to: further examine recommendations from the IWA [‘Funding Renewable Energy Projects in Wales’] report, prioritise next steps and develop a collective action plan. The aim of the Re-energising Wales project is to provide a fully worked out plan to enable Wales to meet its projected energy demands entirely from renewable sources by 2035, resulting in an 80% reduction in energy-related greenhouse gas (GHG) emissions.

The report, the first short policy paper of the Re-energising Wales project, was launched in April 2017 and made 18 recommendations that could lead to the development of more investment in renewable energy projects in Wales. Shea Buckland-Jones, Re-energising Wales Project Coordinator, gave an overview of the report’s recommendations and its largely positive reception amongst partners. The IWA have also held constructive conversations with a range of organisations including Welsh Government, Natural Resources Wales and community partners.

Shea Buckland-Jones also gave an overview of the current context, including the timeliness of the pension fund recommendations given that a large percentage of local government pension fund assets in Wales will be part of a shared pool by April 2018. Shea articulated his hope that the discussion would help tease out the challenges and opportunities relating to pension funds and community energy schemes in particular, to allow the group to identify collective actions, potential quick wins and longer term activity.

A minutes silence was held at 11am for victims of terror attacks in London on 3rd June 2017.

Session 1: Pension funds

Debbie Fielder and Yvonne Keitch set the scene for the session by giving an overview of their experience working within local authority pension funds in Wales. Debbie Fielder, speaking on behalf of Clwyd Pension Fund, reflected that the Clwyd fund has been investing in infrastructure for over 17 years. However, many of the local government pension funds in Wales don’t currently invest in infrastructure. As a small team, they have to rely on bringing in expertise from outside to help with investments. This impacts the pension fund's ability to invest in individual schemes such as renewable energy projects. A key barrier to such investments is the support needed with the due diligence decisions required for investment decisions. Debbie reflected that it will take years to develop in house expertise as part of the pooled Wales funds, and there will be a period of time where external support, which is a significant cost, will still be required to assist in particular with the due diligence decisions required. Debbie questioned whether the pooling of funds will create an opportunity to share the cost of due diligence of alternative Fund Managers, as this is a key challenge for small local authority pensions teams in Wales.

The Wales pool intends to transition listed equities and fixed income, approximately 80/85% of total assets, onto the Authorised Contractual Scheme (ACS). Limited partnerships such as infrastructure do not usually fit into an ACS structure, therefore these may take longer to pool whilst an alternative structure is determined.

Yvonne Keitch reflected that there are significant differences between local authority pensions funds, in size and approach, throughout Wales. This in turn impacts required risk and return profiles and different approaches to investment strategies. Reflecting the UK Government's drive for pension funds to invest in infrastructure, as an example, the Clwyd Fund aims to reach a 7% investment in infrastructure by 2020. Pooled funds are likely to set targets for infrastructure investments. This does not mean investment in infrastructure in Wales however and there is currently no detail within the Wales pool tender regarding delivery of social and local benefits. Yvonne reflected that there is a significant opportunity for economies of scale with the pooled funds, particularly on the cost of external support.

The discussion was then opened up to the group and a range of pertinent issues raised, including the scale of investment which local government pension funds can make in any one project or fund, to help spread risk. Debbie noted that Clwyd Pension Fund infrastructure investments for the previous 2 years had returns of around 20%, compared to around 15% for private equity investments, and although the fund has invested in renewables, it was too early to analyse those returns. Clwyd have already been reducing exposure to public equities, currently at 14% of the portfolio compared to the LGPS average of 60%.

James Thelwell, GLIL Infrastructure LLP, reflected on his experience of pooled funds in Manchester, in which each fund put £250 million in a collective pot and 2-3 members of staff. Of 3 investments made to date, 2 have been in renewable energy schemes. To date only partners who can commit personnel have been able to join, but they are currently exploring options for members unable to commit staff resource. Debbie noted that

Clwyd Pension Fund would still have to carry out the due diligence and it's associated costs if investing in GLIL.

Sophie Howe, Future Generations Commissioner for Wales, raised the issue of accountability and where decisions regarding investments are made. Fund Committees comprising of Councillors, amongst others, drive strategies for investment for local authority pension funds, based largely on advice from external professional advisors. It was suggested that this may be a focus area to build capacity and expertise in house, particularly in the principles of the Well-being of Future Generations Act, to increase confident decision making, due diligence capacity and investment in renewables. It was suggested that Welsh Government may have a role to play, with others, in building capacity. It was questioned whether the Welsh Government carbon budgeting role will flow down to impact local government investment. It was suggested that we might be some way from this yet, although Mark Drakeford, Cabinet Secretary for Finance and Local Government, was committed to the carbon budgeting process.

Eurfyl ap Gwilym, IWA Board Member, reflected on his experience of running a private pension fund and the usefulness of a "statement of investment principles" for clear decision making. Clwyd Pension Fund, as well as all other LGPS funds, have an investment strategy statement. It was suggested however that the Well-being of Future Generations Act guidance may help form a template for such a document for pooled local government pension funds in terms of driving investment decisions. Eurfyl also reflected that there is a danger in becoming too dependent on outside advice with no longer-term benefit, and it was important to build capacity within local authorities.

Auriol Miller asked the group to consider recommendations 5- 10 and share their reflections. Bruce Davies, Abundance Investment, reflected that co-investment (recommendation 10 of the IWA report) is a familiar challenge because there is a lack of shared understanding between parties about what pension funds are there to do. Bruce asserted that there is no mechanism for pension funds to invest alongside communities, and this is a significant gap. A joint venture set up could help drive this co-investment.

Helene Winch, HSBC, identified that new guidance to Local Government Pensions Schemes from the Department of Communities and Local Government very clearly requires English and Welsh local pension schemes to determine what they are doing regarding climate change, and this may be a helpful driver for investment in renewables for pooled funds moving forward. The Pensions Regulator were identified as a key partner in driving this forward. It was also noted that the Financial Stability Board, which advises Mark Carney at the Bank of England, also have to report on accountability regarding climate change when following guidance. The Environment Agency pension fund were identified as a useful example to learn from as the fund is divesting its fossil fuel assets and it has a 15% target for investment in low-carbon energy, energy efficiency and other businesses that help tackle climate change by 2020 and each financial manager has to complete a carbon footprint on their investments to help avoid carbon risks. The Green Investment Bank and European Investment Bank also have clearer reporting mandates in this respect. Helene shared that HSBC are also working on carbon footprinting, and her experience is that alternatives to carbon heavy investment are now the same price. There was a brief discussion about products and vehicles more suited to the market, and it was suggested that ISAs may be a more useful form of investment for community renewables.

The group reflected on the interaction between guidance from the Department for Communities and Local Government (UK) and the Well-being of Future Generations Act (Wales), and the need for local government pension funds in Wales to take account of both sets of legislation/guidance. Jonty Graham, Foresight Group, raised the issue of fiduciary responsibility which would also interplay, and the need for guaranteed return possibly has primacy over other duties. It was also noted that the Financial Conduct Authority now has a public value test, which is yet to be defined but will also impact on decision making. Auriol identified that this presented an opportunity for the IWA to convene partners to do some fact finding on the current state of play and what it could look like in the future. Jennifer Pride, Welsh Government, reflected that the responsibility and accountability on these issues is a jigsaw and that we are on a journey to build capacity and expertise. Jennifer also shared that there is a Cabinet Sub Committee looking at Carbon budgeting. Auriol Miller, Chair, summarised the conversation as identifying shared confidence that the processes and requirements are there, but confidence and capacity are still to be built up.

Session 2: encouraging investment in community energy schemes

Dan McCullum, Awel Aman Tawe, introduced this session by describing his experience and perception of the challenges in securing investment in community energy schemes. He described how the planning and funding systems can be very challenging to navigate, procurement is a big risk and that control of land is a critical issue. He credited Welsh Government support, and support from trusts and foundations, as being critical in matching the community share offer he devised, which raised £2.3 million. Later Dan gave an example of other cooperative groups who have developed bond schemes to help raise money. Dan argued that there should be a discretionary element within pension funds to fund community schemes. He also reflected that now subsidies have been taken away from renewable energy, there may be more scope for community groups to acquire land. This challenge was repeatedly recognised throughout the discussion.

Driving investment

The discussion was opened to the group, and focused initially on the recent Natural Resources Wales tender and whether there were any specific requirements on co-benefits to help drive joint ventures between for example, larger developers and community groups, so that community groups could have ownership stakes in projects. The group heard that the main tender requirement is a total return of revenue, however environmental and wellbeing implications are also taken into account.

Models of supporting community energy schemes in Germany were given as an example of good practice and the learning would be good to reflect on in Wales. Two possible solutions were proposed: exploring joint ventures with bigger companies, and bringing in external commercial expertise to support community led projects.

Jeremy Smith, Innogy, reflected that the risk of regulatory change on renewables during development is a very real risk and that they had lost projects mid development. Jonty Graham, Foresight Group, agreed that institutions are very risk averse and that the rate of development in renewables is so fast paced that institutions are unwilling to take risks of unproven developments without subsidies. He questioned whether there is a way of insulating the risk to investors over the longer term. New York Green Bank were suggested as an interesting group to speak to on how they approached and managed risk in this area. A vehicle could be set up to help with risk. This could be particularly helpful in a world without subsidy for renewable energy, in needing something to guarantee long term assurances to reduce development risks. Without subsidy, how 'Power Purchase Agreements' will look is a challenge.

Professor Calvin Jones identified the potential opportunities arising from the proposals for a National Development Bank in Wales, and whether there is an opportunity to positively influence that development through the IWA. Further examination of the provisions of the Wales Act and powers over energy is required to pursue this.

Michael Brown argued a successful approach is about structuring risk and recognising that different types of capital come in at different phases in a project cycle. He argued that mezzanine funding can help de-risk the early stages where there is limited capital requirement but high risk. Who takes the risk and where does it sit? It was noted that this is where Welsh Government intervention is most helpful and can help unlock cheaper capital later on.

Bruce Davies argued that there is a need to better understand the life cycle of risk and funding, and learn lessons about how to make community energy projects programmable and replicable, whilst acknowledging all communities are unique. He reflected that the focus tends to be on the set-up, not the longer term, and there is a need for a more sophisticated approach that included different approaches, correct governance structures and organisations at different phases in the project cycle. He argued that a much neglected area is end responsibility. Bruce noted that Abundance went through the FCA with this in detail in order to help build the business case to talk to retail investors and others. Bruce also reflected that the largest institutional investor he works with is a Building Society, who are better structured to expose themselves to these types of investments. It was noted that the IPA treasury has established models for setting up layers of ownership, but to date these have not been applied to community energy in a systematic way.

Keith Jones shared information about work done by ‘Forum for The Future’, who are doing some work around community asset banks and driving community ownership of large schemes and assets on sites. They are 3 months into this project and they have a team of lawyers looking at what is stopping investment, and what are the mechanisms for conducting due diligence. It was noted that the motivations of community energy projects and investors are often very different, which for investors presents a significant risk. It was noted that social investment tax relief would offer a significant incentive. Furthermore, cooperatives have raised money through bonds and the community sector needs to be more open to new ways of securing finance. Equity and debt should be mixed better by community groups as well.

Jennifer Pride articulated that Welsh Government are focusing their efforts on learning more about the shared ownership process, so are bringing the right people together in the right place and the right time to help promote shared ownership and ways of doing it efficiently. The group acknowledged that it is important to look at communities in the broadest sense, including the people who live there but also the people who care, and take an asset based approach to community projects.

Incentives

Keith Jones, National Trust, identified that the the Plant Machinery Act and the recent business rates review calculated by the Valuation Office Agency, are huge barriers to the community energy sector. The way business rates are calculated means hydro schemes are hit hard as unlike most businesses, machinery used to generate power is included in the valuation. Keith noted that there have been 3 appeals in Scotland already on the way rates are calculated. It is assumed that the majority of the capital expenditure in delivering the schemes has been paid by the owner of the land, whereas it is the hydro's operator that usually pays and no allowance is made for the fact they are often run by volunteers. Meanwhile, schemes cannot increase the amount of money they make because they have a set rate for the power they generate.

Keith stated that some sites have seen a 233% increase on their previous rates, and it is disproportionately affecting newer sites over 70 kwh who are not eligible for small business rates relief. He asserted that legislation change or discretionary power business rates relief support is needed to help this situation, but that in the current political climate there was little room to prioritise these. Keith noted that hydro needs a level playing field with other technologies, arguing no one could afford to put such a significant amount of their costs on business rates.

Keith reflected that Scotland have introduced relief that lasts for a year, and England have capped rates. He argued that this has stopped development for the community energy sector in Wales, and that 14 projects have ceased since this came into place. He gave an example from Bethesda in which 100% of their profit, which usually goes towards community benefits, will go to the paying their rates to the local authority.

Jennifer Pride advised that Welsh Government are presently trying to collect evidence on the impact to develop and inform a long-term solution. The challenge largely lies in the legislation. They have set up a working group to examine the issues and business models, in particular why the hydropower sector is so adversely affected and the cost of a relief scheme. It was noted that the investment model for hydro power doesn’t take into account that projects can last 100+ years, and so it is unreasonable to expect repayment in full within far less timescales.

Social investment tax relief was raised again as an issue for examination, in particular the measurable impact and outcomes of doing good. Keith Jones noted a PHD being undertaken with Welsh Government looking at the wider impacts of community energy schemes such as the social impacts and future generation impacts which could be useful in this respect. It was noted that non financial factors being take into account by a range of sectors still largely focused on economic impacts such as job creation. The inclusive economy unit within the Treasury is reportedly doing work on the repurposing of funds and improving structures for investment. Jonty Graham reported that there are advanced measurement tools available to measure non-financial impact that are widely accepted. Bruce Davies, Abundance investment, advised that he led a study on the Swansea Bay Tidal lagoon to examine how this could be a genuinely community owned led project. Auriol identified that the IWA would follow this up as an example of relevant research for the Re-energising Wales project.

In concluding this session, it was acknowledged that a mapping exercise was needed to identify what is out there in terms of successful community energy projects, the support they received and models they utilised.

The broader context: investment opportunities in the short to medium term

The group identified the role of smart cities and city region developments as a priority opportunity to support investment in community energy schemes. It was noted that Swansea are more actively considering energy than Cardiff at present, but that the time to help shape developments and secure solid proposals in renewables is now. In securing money for digital developments, it makes sense to tackle energy developments at the same time e.g. LED street lighting (which the Green Investment Bank have offered funding for recently). Energy efficiency should come first. Jeremy Smith noted how Glasgow have developed electric vehicle charging points on the back of smart city funding.

In concluding the event, the group supported the idea of reconvening in the near future to examine progress and further develop potential solutions. Key issues for further examination included:

- Consideration of how renewable projects can be financially underwritten in needing something to guarantee long term assurances to reduce development risks
- Opportunities for further developing onshore wind projects in Wales
- Industry working in partnership with community schemes and exploring innovative funding models, including keeping an eye on the result of the Natural Resources Wales joint venture tender noted above and its future impact
- Linking with ongoing work of the UK Government in thinking about a route to market for renewables post election
- Energy has come through as a potential key issue in the priorities work of the Future Generations Commissioner for Wales, who are currently working to analyse/prioritise these issues and confirm themes soon

- Greater consideration of SRI in pension fund decision making; greater examination of how to best respond to the different stages of a project life cycle; could pension funds set discretionary amounts for community energy projects?
- Improving communication between the various partners involved in community energy schemes and pension funds. A mechanism such as a joint venture set up could help drive this co-investment.
- Learning from Abundance Investment in terms of not just focusing on the set-up of a project when getting funding, but also on the longer term and end responsibility, in needing to take a more sophisticated approach that includes different approaches, correct governance structures and organisations at different phases in the project cycle. Abundance went through the FCA with this in detail in order to help build the business case to talk to retail investors and others. The IPA treasury has established models for setting up layers of ownership, but to date these have not been applied to community energy in a systematic way.
- The community sector needs to be more open to new ways of securing finance e.g. cooperatives have raised money through bonds

Agreed actions

- Auriol and Sophie Howe to discuss opportunities for mutual support on these issues, once the strategic process for the Future Generations Commissioner has completed. This could include increasing due diligence capacity within pension funds, ensuring funds take account of the Well-being of Future Generations (Wales) Act 2015 and devising templates for driving investment decisions amongst other things
- Explore shared ownership opportunities further after the NRW tender decision. Community energy projects to get involved in bigger projects.
- Debbie to share as much information as possible moving forward on the pension fund pooling process, including how to influence the process
- James Thelwell to follow up conversations with Welsh Pension Funds to discuss how they can share mutual expertise and learning
- Helene Winch to share information about the Re-energising Wales project in a paper she is writing for the Green Finance Initiative on 21st century infrastructure, due to be published in September 2017 when there is a Green Equities conference
- Attendees to make further links with large institutional investors, with Building Societies mentioned as investors who are well structured to expose themselves to these types of investments

- Bruce Davies to share a study on the Swansea Bay Tidal lagoon which examined how this could be a genuinely community owned led project
- IWA to follow up suggested useful conversations with the Pensions Regulator and the Environment Agency
- IWA to clarify the provisions of the Wales Act on energy schemes
- IWA to work with partners in further examining the impacts of the business rates review on hydro schemes
- The IWA to develop links with ‘Forum for The Future’, who are doing some work around community asset banks
- The IWA to consider existing mapping exercises that identify what is out there in terms of successful community energy projects, the support they received and models they utilised.
- IWA to reconvene this group in the medium-term with the purpose of examining progress and further developing solutions