

AGREEMENTS REVIEW

1. BACKGROUND

- 1.1 Colchester Amphora Energy Limited (“CAEL”) was set up as part of the planned Northern Gateway project to deliver a low carbon heat network for residents, businesses and other commercial users (the Northern Gateway Heat Network or “NGHN”). CAEL is a wholly owned subsidiary of Colchester Commercial (Holdings) Limited (“CCHL”) which in turn is wholly owned by Colchester City Council (“Council”).
- 1.2 Due to the uncertainties surrounding the delivery phasing and dates of the Northern Gateway project, it has been decided to make CAEL dormant because it has no current or medium term prospect of being able to continue to meet all its liabilities without relying on shareholder support. There are also benefits to bringing arrangements to a close from an accounting perspective for the Council.
- 1.3 The objective is for the benefit of CAEL’s assets and existing agreements to be transferred to the Council. This will preserve flexibility for the Council, allowing a decision to be made about the extent to which the Council or its companies wish to be involved in future Northern Gateway infrastructure provision. The Council has asked for six agreements to be reviewed and for AC to set out the actions needed to achieve the objective.
- 1.4 There are two legal terms used in this report which describe how arrangements which have previously been made by CAEL may be “transferred” to the Council:
 - 1.4.1 An “assignment” is where the legal benefit is transferred to a party where there are no actions or live obligations to be fulfilled under the contract. The party to whom the benefit has been transferred can then use that benefit – for example a benefit of most contracts is to be able to enforce them if a supplier has not complied with its obligations.
 - 1.4.2 A “novation” is where all the parties must agree (the supplier, CAEL and the Council) to change the “customer” from CAEL to the Council. This is to be used where the Council needs to continue to order services or goods from the same supplier.
- 1.5 The recommendations for the reviewed agreements are either to assign, novate, leave alone or suspend. Each agreement needs dealing with properly to ensure that there are no questions left about CAEL’s obligations or the Council’s rights and responsibilities in future.

1.6 This advice does not factor in tax issues, and you have confirmed that the Council and Amphora group of companies will obtain separate advice about progressing the objective in a tax efficient manner. If a tax adviser has any comments on our proposals for each of the agreements, AC will gladly collaborate with them to ensure that the most efficient result is achieved.

2. HEAT PUMP AGREEMENTS

- 2.1 A fourth version of the proposed tender by GEA dated 6 March 2023 has been provided for review (“the Fourth Tender”) and it is assumed that this is the final version accepted by CAEL. The Fourth Tender only specifies “Amphora” as the customer (and not specifically CAEL), however it lists as being for the attention of Michael Woods – an employee of CAEL so it is reasonable to imply that CAEL is the customer.
- 2.2 The Fourth Tender states that a deposit of £165,732 was paid to GEA on 16 August 2021 and that the delivery date may not be until Q1 2025 due to the NGHN project delays.
- 2.3 A report by the Chartered Institute of Public Finance & Accountancy (“CIPFA”) dated January 2023 states that CAEL intended to novate this agreement to Pinnacle. Pinnacle is a contractor which was successful in CAEL’s procurement process for its requirements to construct an energy centre and to provide operations and maintenance for the NGHN. However, the Fourth Tender should be novated to the Council because it is unlikely that Pinnacle will be appointed at all as it is probably now too long since the conclusion of the tender process to rely on the result (see below).
- 2.4 As part of the novation, the Council would need to pay CAEL an amount to reflect the deposit already paid. The Council would then be required to pay the remainder of the purchase price to GEA at the relevant times set out in the Fourth Tender and GEA would act as if the Council had been the purchaser from the start of the transaction. Under the Fourth Tender the next payment, of 40% of the purchase price, is due at delivery of the “*main parts of the Scope of Supply to [the] Site*”.
- 2.5 The Council could consider whether or not to continue with the purchase of the heat pump altogether, instead of perusing novation, particularly if the future of the NGHN is unclear. GEA’s terms do not appear to give a right to cancel the order, but if this is potentially preferred position, careful negotiation would be needed to discuss this with GEA without causing contractual issues. It is acknowledged by CAEL that the terms of the heat pump purchase were not ideal – indeed there are very strict caps on GEA’s liability. This is because the purchase was concluded under considerable time pressure. It might be possible to negotiate the return of some of the deposit if there is goodwill from GEA if the manufacturing of the pump has not progressed. More information about this would be needed to see if there is any realistic prospect of such a negotiation succeeding.

- 2.6 To the extent that parts of the heat pump or any other equipment has been delivered, a sale and purchase agreement should be concluded between the Council and CAEL to transfer these assets. It might be appropriate to incorporate the sale and purchase terms into the novation agreement instead of having a separate agreement. This is a detail that can be worked out later.

3. DEVELOPMENT MANAGEMENT SERVICES

- 3.1 A development management services agreement has been entered into between the Council and CAEL dated 20 December 2019 (“the DMSA”). As part of the DMSA, CAEL is providing a wide range of management and design services to the Council. Whilst CAEL itself was carrying out some of the management function, it was sub-contracting much of the design to WSP.
- 3.2 Once CAEL is dormant, there will be no further services carried out under the DSMA. As the Council already has the benefit of this agreement, and there doesn’t appear to be any advantage in novating it to any other Amphora Group companies, the other options are to not do anything, or suspend or terminate the DMSA. If nothing is done, the DMSA is just left “hanging”, with neither party carrying out its obligations, which is unhelpful from an audit and legal perspective. To preserve future flexibility, all of the DMSA obligations could be suspended under clause 9. The Council can issue an instruction to suspend – this will trigger a requirement to pay CAEL up to the date of suspension. The Council has the right to re-mobilise the services if it wishes in future, but if not, the suspension can last any period until the Council decides how to re-procure the NGHN in future. Once 9 months of suspension have elapsed, the Council can terminate if it wants to, or if there are strong views it should be terminated now, the DMSA could be terminated now by agreement.
- 3.3 The DMSA has some key provisions missing, such as a copyright licence back to the Council and was said to be executed as a deed, but it does not comply with the required formalities so will take effect as a simple contract. Bearing in mind the relationship between the parties, neither of these issues is a significant problem but should be rectified if any further services were ever provided under the DMSA.

4. TECHNICAL CONSULTANCY - WSP

- 4.1 Pursuant to a tender response document dated 12 October 2018 (“the Tender”), WSP has and continues to provide consultancy services including the CDM principal designer role in relation to the NGHN. The services that WSP provided ranged from developing the technical specification, to modelling, and in future, project management during the construction phase.
- 4.2 It does not appear that any formal agreement was entered into between WSP and CAEL. An unsigned framework agreement has been provided with the Greater London Authority stated as the contracting entity alongside the Tender.

- 4.3 Although not an immediate risk to the project, it would be strongly recommended for CAEL to have an executed formal appointment of WSP. The framework terms deal with this by providing a template for this at Schedule 6A of the framework. This will ensure certainty as to the terms of the appointment and it should ideally be executed as a deed, both ensuring greater protection for CAEL and the Council. From a brief review, unfortunately the framework agreement and the Schedule 6A terms are missing key points (such as Construction Act compliance, CDM and copyright licensing) but this should be rectified when the appointment is formalised.
- 4.4 We assume that WSP's involvement in the NGHN is still ongoing, and that the Council wishes to retain WSP's services for future development of the NGHN. The agreement between CAEL and WSP can be formalised and novated to the Council all in one document.
- 4.5 As WSP planned to use a sub-contractor, Norr, to provide architectural services for the energy centre, collateral warranties should be required when Norr is appointed by WSP. However, there does not appear to be provision for collateral warranties in the WSP arrangements so this should also be remedied on novation.
- 4.6 If the Council does not formalise the appointment, then this may cut down its options in terms of later passing risk to the market. If the Council (or any Amphora Group company) were to take the project forward, it might be under a master concession arrangement with an external provider, such as Vital or Pinnacle. In this instance, the benefit of all the WSP work and contract would need to be transferred to that new entity, if indeed the objective were to pass the design, construction, operation and maintenance on to a single responsible external entity. That single entity would not currently accept a novation or assignment of a non-formalised appointment. Formalising the appointment is also required as part of the Council's contracts procedure rules.

5. FACILITY AGREEMENT

- 5.1 A facility agreement, providing a loan of up to £2,250,000 has been entered into between CAEL (as the borrower) and the Council (as the lender) dated 25 June 2019 ("the Facility Agreement"). A fully executed copy is not available but it may have been executed in counterpart. It is understood that approximately £1.3million has been drawn from this facility.
- 5.2 As part of the Facility Agreement, CAEL entered into a debenture with the Council dated 25 June 2019 which was executed in counterpart ("the Debenture"). The Debenture provides CAEL with a first legal mortgage over "*all estates or interests in any freehold, leasehold or commonhold property now owned by it...*" (clause 3.1), which also includes "*all buildings and fixtures and fittings...*" (clause 1.4(a)).
- 5.3 Once CAEL has been paid under the DMSA for all the management and design services it has provided up to date, and has been paid for all the other assets (such as

the GEA order) which are being transferred to the Council, it is likely that CAEL could then pay back the Council the borrowings under the Facility Agreement. Potentially, there will be some part of the loan which may have to be written off. Once the full amount of cash requirement is known up to the date of dormancy, then the write off amount will be known and at that stage, the Facility Agreement and Debenture could be terminated by mutual agreement. All this should be formalised in a very short deed of termination. Writing off debts is likely to be a financial benefit not given to any other entity so could be a subsidy subject to the Subsidy Control Act 2023 - however, it is assumed that any other market provider of loans would do the same so there is no real concern here.

6. GRANT AGREEMENT

- 6.1 A grant agreement has been entered into between CAEL and the Council, dated 25 March 2017 (“the Grant Agreement”). The Council agreed to provide CAEL with up to £220,000 towards the cost of set up of CAEL and the NGHN.
- 6.2 Clause 6.1 of the Grant Agreement shows that the last instalment of funds would have occurred in the financial year 2020-21, therefore there are no future planned payments by the Council to CAEL under the Grant agreement.
- 6.3 The Grant Agreement allows the funds to be used very broadly in connection with the NGHN, with only limited ineligible expenditures listed within Annex B. We presume the grant has been paid in full and expended by CAEL in accordance with the terms of the Grant Agreement.
- 6.4 The Grant Agreement does not appear to have any restrictions on dealing with assets which have been funded through the grant. This means that the assignments, transfers and novations suggested in this do not need specific Council consent if they relate to supplies, services or works funded by this grant.
- 6.5 As there does not appear to be any breach of the Grant Agreement, and the terms have been fulfilled, there is no particular need to assign, novate or terminate this agreement and it can be left in place during any dormant period.

7. CONCESSION AGREEMENT

- 7.1 A concession agreement has been entered into between the Council and CAEL dated 31 January 2018 (“the Concession Agreement”). The Concession Agreement granted CAEL the exclusive right to supply heat to the individual residential, commercial, retail and/or leisure units to be constructed within the concession area. The Council was required to ensure developers within the concession area entered into a connection and supply agreement with CAEL on terms in accordance with the Concession Agreement.
- 7.2 The Council could terminate the Concession Agreement. Although the termination provisions within clause 11 provide for only termination in the event of non-remedied

material breach and a party exceeding its liability cap, the CAEL and the Council would be able to terminate upon mutual agreement with one another and this should again be recorded in a very short Deed.

- 7.3 The other option is to suspend both parties' obligations by mutual agreement in case the concession agreement could be resurrected in future to be used between the Council and CAEL. Whilst the Concession Agreement was no doubt fit for the early stages of developing the NGHN, it is too lightweight to be used for the next stage. There are insufficient terms dealing with commercial viability in the early years of operation, and insufficient terms around the operation and maintenance of the project. In our view, it is therefore probably advisable to terminate and to put new arrangements in place once the options have been appraised.

8. PINNACLE AND PROCUREMENT

- 8.1 CAEL should clarify whether it has entered into any contractual arrangements or has any obligations towards Pinnacle. We would be happy to review any additional documentation relating to Pinnacle and the heat pump, as CIPFA's comment suggests such documents exist. AC's last involvement in the procurement process was when the procurement was paused after evaluation had been carried out. The procurement process should probably be formally abandoned without award, just so that there is a clear audit trail, and that if the Council or others need to conduct a further procurement process in future, there is no question of a challenge from Pinnacle that has any claims to be awarded the contract under the previous process.

9. OVERVIEW

- 9.1 The below table illustrates a high-level overview of the recommendations for each of the agreements reviewed.

AGREEMENT	RECOMMENDATION
HEAT PUMP AGREEMENT	NOVATE THE AGREEMENT TO THE COUNCIL
DEVELOPMENT MANAGEMENT SERVICES	SUSPEND BOTH PARTIES' OBLIGATIONS
TECHNICAL CONSULTANCY	FORMALISE THE AGREEMENT AND NOVATE IT TO THE COUNCIL – ADD COLLATERAL WARRANTIES AND A NUMBER OF OTHER MATTERS
FACILITY AGREEMENT	DEED OF TERMINATION WHICH RECORDS TERMS RELATING TO WRITE OFF
GRANT AGREEMENT	NO FURTHER ACTION



10. DECISION MAKING REQUIRED

- 10.1 As already advised, a decision to place CAEL into dormancy is a matter for the Council as the ultimate shareholder of the company in accordance with the November 2017 Group Governance Agreement and delegations schedule therein.
- 10.2 The decision will be effected by a (written) shareholder resolution(s) proposed by the CAEL board and circulated in the first instance to CCHL board acting as the 'first instance' shareholder of CAEL.
- 10.3 The operational implementation of the resolutions and thereby CAEL preparing and making all necessary arrangements prior to dormancy will be the responsibility of the CAEL board. There are procedures to be followed for either course of action in respect of which we would be happy to advise further.

11. NEXT STEPS

- 11.1 It is suggested that the implications of the decision to place CAEL into dormancy should now be documented so that all matters can be contained into one report for governance purposes. That report will then be the basis upon which the recommendation will be made.
- 11.2 We would be happy to support the Council and CAEL to implement some or all of the suggested courses of action above once necessary governance is completed. It might be useful to discuss the conclusions and we could attend a brief meeting to check you are in agreement with our advice.
- 11.3 If requested we would be happy to draft the necessary resolutions and cover reports if required from a governance perspective.
- 11.4 Please do not hesitate to contact us with any queries or if any further information is required.

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