SURREY COUNTY COUNCIL

CABINET

DATE:	**25 JULY 2023**
REPORT OF CABINET MEMBER:	**MARISA HEATH, CABINET MEMBER FOR ENVIRONMENT**
LEAD OFFICER:	**KATIE STEWART, EXCECUTIVE DIRECTOR, ENVIRONMENT, TRANSPORT AND INFRASTRUCTURE**
SUBJECT:	**GREEN FINANCE STRATEGY**
ORGANISATION STRATEGY PRIORITY AREA:	**ENABLING A GREENER FUTURE**

Purpose of the Report:

Financing our plans to achieve Surrey's net-zero carbon targets requires a robust and sustainable financial framework.

This report seeks Cabinet approval for the approach set out in the Green Finance Strategy (the Strategy) (Annex A), which builds on and develops the Initial Finance Strategy [1], produced in 2021. The Strategy includes investment principles as well as delivery and governance recommendations to enable the Council to make informed investment decisions to support the delivery of our net-zero carbon 2030 and 2050 targets as set out in Surrey's Climate Change Strategy [2] and the Greener Future Climate Change Delivery Plan 2021-2025 [3]. The Strategy includes a summary of income generation mechanisms which the Council are developing to generate the investment needed to achieve the county wide target and offset costs.

The Strategy also contains an up to date review of costs, focusing on the Council's net zero 2030 programme, which provides an illustration on the quantum of expenditure required to achieve this target and the level of income needed to offset costs together with proposed sources. This report is not seeking approval for the full capital sums included in this summary. An Investment Plan will be brought back to Cabinet in the autumn which will set out the decarbonisation schemes that the Council will be looking to invest in in the next one to two years.

Recommendations:

It is recommended that Cabinet:

1. Agree the updated approach and investment principles, that support the delivery of the Council's 2030 and 2050 net zero targets, as set out in the Green Finance Strategy.
2. Agree the recommended approach option for the delivery of the Council's 2030 net zero target, including exploring and developing additional finance mechanisms to offset potential future costs.

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Reason for Recommendations:

- In the eighteen months since the Climate Change Delivery Plan and the Initial Finance Strategy were published in November 2021, rapidly changing and increasing costs along with learnings from the delivery of capital decarbonisation schemes on the Council's estate, has meant that the Finance Strategy requires updating. This paper, and the accompanying Green Finance Strategy, sets out the updated approach for approval.

- Officers in Greener Futures and Finance with support from Land and Property have been further developing the 2030 finance model, which was originally produced by consultants, in order to gain a more robust understanding of the capital costs required to achieve the 2030 target, as well as the potential to offset these costs through energy savings and income generation. Given the increase in costs, four future approach options have been developed. The recommendation to Cabinet is to adopt the 4th option.

- It should be noted that all options will require the Council to invest money up front in advance of income being generated. Net zero is a significant cost to the council with all options, but the approach is to off set this and aim for cost neutrality over the longer term by generating income through renewables and reducing costs of energy.

1. The Council abandons the 2030 net zero target.
2. The Council only installs decarbonisation measures which have a strong return on investment (such as solar) to reduce capex, accepting that this will increase the cost to the Council for carbon offsets from 2030 onwards. The minimum projected offset costs for this option (to 2050) amount to at least £14m, calculated at a rate of £95t/CO2, however by 2030 this rate may be much higher. This option is therefore not recommended as the financial risk is considered too great and the efficiencies resulting from investment in the more costly decarbonisation measures would not be achieved.
3. The Council builds all the projected increased costs of achieving the 2030 target into the Medium Term Financial Plan, and income is seen as a bonus. This is the approach taken by other Local Authorities however by not pursuing and prioritising investment in renewables, which would generate income, this would lead to a budget pressure.
4. The Council continues with the current approach to achieving the 2030 target, which includes being open and transparent with costings and balancing the delivery of high cost and quick pay back measures. This approach includes the development of finance income generation mechanisms, mainly renewables, with the purpose of generating a return on investment to offset any future potential cost increases to the Council, or to be used for other Greener Futures priorities.

Executive Summary:

1. The Climate Change Delivery Plan (CCDP) 2021-2025 sets out the recommended net zero delivery pathways for both the Council's 2030 net zero carbon target and the 2050 net zero carbon target for the County. In 2021 the Greener Futures Team were asked to estimate costs and set out how these targets would be financed. This information was included in the Initial Finance Strategy (2021) on the understanding that the work would be further developed at a later date due to complexities.

2. To inform the Initial Finance Strategy, consultants Atkins were commissioned to produce two finance models for the 2030 and 2050 carbon targets. Based upon the summaries from these models, Cabinet agreed that the Council would play an active investment role in the SCC 2030 target, committing its own funds to the decarbonisation work required, and more of a facilitation role in the Surrey 2050 target drawing in grants and resident/business investment. The 2050 model will be further developed by officers before the end of the financial year.

3. In the last six months the 2030 finance model has been developed by officers in Finance and Greener Futures, with input from Land & Property and other teams in order to create a more robust framework for decisions. The model is based on the premise of cost neutrality, so the capital costs are offset by energy savings and income from renewable energy. The model is technically complex and is underpinned by a number of factors, none of which are static. This means it will continually evolve.

4. It should be recognised that the total cost of achieving the net zero 2030 target is estimated at between £88 - 109M, which is an increase from the original model. Many of these costs relate to improving existing building fabric and for measures which have benefits above and beyond carbon reduction. For example, replacing single glazed windows with double glazing and replacing old and inefficient heating systems with low carbon heating and cooling systems will improve the condition of the buildings, increasing its value as well as creating better working environments for staff.

5. Despite the capital cost increases mentioned above, the opportunities for savings and income has also increased. As a result, the modelled Net Present Value of the 2030 programme (to 2050) is positive, and the project is predicted to pay back in 26 – 28 years.

6. It is important to note that, as a precaution, the 2030 model contains pessimistic costs and there are several factors which could improve the financial position of the model. However, these figures are underpinned by savings and income targets that must be achieved for this to happen.

7. It should be recognised that there will be considerable up front cost and that income and energy savings will be realised on a longer term basis. In order to reduce the risk to the Council, a 2030 Greener Futures Investment Plan will be produced and brought to Cabinet in the autumn. This Plan will outline the capital decarbonisation schemes in train over the next two years and when the investment for these will be needed. This Plan will form part of the Council's financial planning process, which will ensure that there is a balance of measures that do not over commit the Council at any given time.

8. More broadly the Council's ability to lead on carbon reduction to achieve the Council's 2030 target and influence and enable carbon reduction at the county level, to support the delivery of the county wide 2050 target, is very much dependent upon the decisions, finance mechanisms, funding and national infrastructure put in place

by Government. This risk is included in the risk assessment within the Green Finance Strategy.

9. To reduce risks around financing, officers are currently exploring and developing several finance mechanisms which have the potential to draw in investment and/or generate income essential to offset costs and support the delivery of the 2030 and 2050 net zero carbon target. A summary of the more mature mechanisms is included in the Finance Strategy and includes;

- A solar power purchase agreement (PPA)
- SME green business loan scheme
- Household decarbonisation loan scheme and one stop shop for domestic retrofit
- Carbon offset/inset opportunities

10. The Green Finance Strategy, and the models which sit beneath it, enable the Council to take a pragmatic approach to decisions around carbon reduction, factoring in value for money. When developing business cases officers from all the relevant services, supported by the Greener Futures Group, will consider whether the decarbonisation project represents value for money against a number of criteria (such as cost per tonne carbon saved, payback years, availability of grant funding, co-benefits (ie energy savings). If the costs are too high, and the carbon savings too low, then the project will be amended or will not proceed. Officers are currently developing a mechanism to help determine whether the project represents good value for money for the amount of carbon that it reduces.

11. Due to technical and financial restrictions it is acknowledged that it will not be possible for the Council or the county to be completely carbon free by 2030 and 2050 and so carbon offsetting will be necessary. It is our ambition to limit the need to offset carbon but where that is not possible we will work with Government and partners to develop good quality carbon offsets which align to Surrey's Greener Futures objectives, such as local nature recovery, and which will benefit the county.

12. As it will be impossible to completely reduce the Council's emissions from all sources by 2030, estimated carbon offset costs are built into the Finance Model from 2030 to 2050 as a revenue cost to the Council. These offset costs would be higher if the Council were not to adopt option 4 (above).

13. Officers will continue to explore and model carbon offset impacts and to ensure these are built into the finance models. The volatile nature of offset markets introduces uncertainty into long-term planning and budgeting. Currently, the lowest traded carbon price stands at £95t/CO2, and it is expected to steadily increase. It is expected that by 2030 the carbon offset cost per tonne of carbon will be much higher due to demand (as a significant number of organisations have set 2030 net zero targets) and increased competition for land/schemes which meet offset certification requirements. Government's UK Green Book for 2030 sets a valuation of £420t/CO2, however offset costs could be even higher by 2030.

14. Target progress against both the 2030 and 2050 programmes will be monitored, evaluated and reported annually to Cabinet and more frequently to relevant member/officer boards and groups in order to comprehensively manage risk.

Consultation:

15. The Strategy and review of costs has been jointly undertaken by Greener Futures, Land and Property and Finance officers. The financial model was updated through the provision of the latest actual project costs, alongside updated cost estimate and changing market and delivery conditions from a wide range of sources.

16. The principles, approach and cost review has been approved through the 2030 and 2050 Climate Change Boards, the Capital Programme Panel and CLT prior to Cabinet.

17. Relevant Cabinet Members have been kept sighted on the development of the Strategy through Asset Strategy Board and the Greener Futures Member Reference Group, which was also attended by Members from the Resources Select Committee with an interest. The Strategy was taken to CEH Select Committee on 5 July 23.

18. As this a strategy for internal use only, stakeholders outside of Surrey County Council have not been formally consulted, with the exception of Borough and District Officers where the Council's investment decisions may facilitate the delivery of climate reduction in other Local Authorities and across Surrey.

Risk Management and Implications:

19. The financial reviews of both the 2050 and the 2030 net zero carbon programmes have identified several key risks (summarised below) that have the potential to affect the pay back of programmes. The risks will require ongoing monitoring and management and as a result governance mechanisms at programme and cross-departmental levels have been set up. The governance approach enables risks to be identified, mitigated and, where necessary escalated.
    (1) The uncertainties inherent in predicting likely changes to prices, borrowing rates, supply chain constraints will be managed through the annual review of costs that forms a key part of our governance process, more frequently at officer level.
    (2) Where the cost of delivering net-zero has the potential to impact services, net-zero options are designed in early, which will reduce additional costs later and allow for informed decision-making with high quality cost and carbon information.
    (3) Risks that projects will not deliver carbon and energy savings anticipated is being managed through active monitoring of projects delivered and a developing approach to offsetting.
    (4) Innovative finance mechanisms that hold significant commercial risk for the Council will be piloted before full-scale roll out.
    (5) Obstacles and challenges that require Government intervention, such as grid restrictions which are delaying or increasing the costs of installing renewable energy schemes, will be built into the Greener Futures lobbying approach. Our approach is to work in partnership with representative networks such as the Local Authority ADEPT network and the County Council Network to escalate issues.
    (6) We will always be mindful of the cost of inaction and where investment in Greener Futures measures could avoid future cost increases through offsetting or potential carbon taxes.

Financial and Value for Money Implications:

20. The objectives of the Green Finance Strategy align to the Council's commitment to deliver value for money for residents and ensure that the Council continues to operate within the confines of what is affordable. The objectives of the Strategy are listed below.
    - An evidence-based estimated cost, based on current knowledge, data and modelling for the net-zero pathways set out in in Surrey's 2050 Climate Change Delivery Plan 2021-25 and SCC's 2030 target.
    - A framework on how investment decisions are made utilising relevant budgets and external funding sources to achieve the climate change programme objectives and minimise financial risk to the Council.
    - A process for refining the 'net-zero pathway model' to confirm, as far as possible, best value measures, costs, funding/financing sources and return on investment for achieving the 2021-25 Delivery Plan and subsequently to be used to define future five-year delivery plans to 2050 and 2030 and their associated investment needs. The model is flexible to allow for different measures if circumstances change.
    - An overview of funding sources and potential finance mechanisms available to fund the delivery of the chosen pathway and more importantly any funding gaps that there may be.
    - The basis of an evidence-based 'ask' of Government with regards to future funding and finance where there are gaps

21. Much work has been undertaken by officers in Finance and Greener Futures to create a more robust and sustainable financial framework for the Council's 2030 net zero target by reviewing testing, developing and updating (with actual commercial costs and sensitivity analysis on energy and borrowing rates) the finance model produced by consultants Atkins.

22. This work has given the Council an indication on the quantum of investment required (between £88 - 109M), some of which will be in advance of income being generated, however it equally shows that this investment could be offset by energy savings and renewable energy generation over the programme period (to 2050) and that the Net Present Value of the programme is positive and the project pay back is between 26 – 28 years.

23. As the financial landscape is constantly changing the model will continue to be updated by officers and officers will report quarterly to relevant boards as well as producing an annual Climate Change Delivery Plan Cost Review for Cabinet.

Section 151 Officer Commentary:

24. Significant progress has been made in recent years to improve the Council's financial resilience and the financial management capabilities across the organisation. Whilst this has built a stronger financial base from which to deliver our services, the increased cost of living, global financial uncertainty, high inflation and government policy changes mean we continue to face challenges to our financial position. This requires an increased focus on financial management to protect service delivery, a continuation of the need to be forward looking in the medium term, as well as the delivery of the efficiencies to achieve a balanced budget position each year.

25. In addition to these immediate challenges, the medium-term financial outlook beyond 2023/24 remains uncertain. With no clarity on central government funding in the medium term, our working assumption is that financial resources will continue to be constrained, as they have been for the majority of the past decade. This places an onus on the Council to continue to consider issues of financial sustainability as a priority, in order to ensure the stable provision of services in the medium term.

26. The Greener Futures finance strategy sets out estimated costs and funding for the 2030 Greener Futures programme, as well as potential financial risks and sensitivities. The current assessment of capital spend required to deliver the programme is £88m to £109m, which is set out in the Greener Futures Finance Strategy at Annexe A and it should be recognised that costs will be incurred up front before any substantial income is generated. Investment will be through a series of at least two year programmes so the financial risk to the Council can be managed and mitigated.

27. However, over the longer term, based on the assumptions set out in the strategy, there is potential to offset those costs, either through reductions in energy costs arising from green investment or from renewable energy generation so that over the longer term there is an expectation that savings and income will be sufficient to offset capital costs, with "payback" (i.e. the point at which savings and income are sufficient to offset investment) achieved around year 26-28. This position is heavily dependent on significant income from ground mounted solar or alternative investments, and may change as the programme and external factors continue to evolve, for example changes in borrowing rates or the cost of equipment. The position will therefore be updated and reviewed, including an annual financial review presented to Cabinet. The estimated financial impacts will be incorporated in the Council's Medium Term Financial Strategy.

Legal Implications – Monitoring Officer:

28. There are no significant legal implications at this stage.

Equalities and Diversity:

29. The Green Finance Strategy is a key part of the *Greener Futures Climate Change Delivery Plan 2021-2025* approved by Cabinet in October 2021. An Equalities Impact Assessment was conducted for the Delivery Plan. (Annex C)

Other Implications:

30. The *Greener Futures Finance Strategy* sets out how we can make investment decisions for the *Greener Futures Climate Change Delivery Plan 2021-2025.* The implications of delivery this plan were considered when it was approved in October 2021 so have not been considered in more detail in this report.

Area assessed:	Direct Implications:
Corporate Parenting/Looked After Children	No direct impact
Safeguarding responsibilities for vulnerable children and adults	No direct impact

Environmental sustainability	Environment Sustainability assessments are not relevant to this Strategy however may be for the specific programmes and capital schemes included in the 2030 and 2050 programme. This will be assessed as each individual business case is developed.
Compliance against net-zero emissions target and future climate compatibility/resilience	The Greener Futures Finance Strategy sets out how we can make investment decisions for the Greener Futures Climate Change Delivery Plan 2021-2025. The implications of delivery this plan were considered when it was approved in October 2021 so have not been considered in more detail in this report.
Public Health	No direct impact

What Happens Next:

31. If agreed the next steps will be to:
- develop a 2030 Investment Plan, to include decarbonisation schemes that the Council is planning to invest in over the next one to two years, for Cabinet approval in autumn of this year
- continue to develop the 2030 and 2050 finance models, feeding in commercial data (including costs) and carbon offset implications, to improve accuracy
- commission consultants to undertake an audit review of the assumptions and data in the 2030 Finance model
- develop an internal carbon benchmark to effectively demonstrate the value for money achieved through decarbonization projects. This benchmark will serve as a valuable tool for assessing and quantifying the cost-effectiveness of our decarbonization initiatives
- continue to develop a longer term plan for all emission reduction schemes required to 2030, in collaboration with Land and Property and in alignment with the emerging Asset Strategy. Once completed a cashflow analysis will be developed against the Plan which will set out when costs are expected to be incurred and when revenue will be generated
- produce quarterly progress reports for CPP, Asset Strategy Board and the Greener Futures Member Reference Group
- continue to develop and test through pilots the finance mechanism included in the Finance Strategy
- undertake a financial review in the next financial year to report to Cabinet which will be repeated annually.

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Consulted:

The Finance Strategy and Finance review were developed jointly by officers in Greener Futures, Land and Property and Finance. The following Boards have been consulted;

- Greener Futures Member Reference Group
- CEH Select Committee
- Asset Strategy Board
- Greener Futures Partnership Steering Board
- Capital Programme Panel
- Greener Futures Steering Board
- Climate Change 2030 and 2050 Boards

Annexes:

Annex A - Surrey Green Finance Strategy

Annex B- Annual Climate Change Delivery Plan Cost Review

Annex C- Equalities Impact Assessment

Sources/background papers:

[1] Cabinet report containing the initial Greener Futures Finance Strategy; October 2021, Item 9 Annex 4; https://mycouncil.surreycc.gov.uk/documents/g7768/Public%20reports%20pack%20Tuesday%2026-Oct-2021%2014.00%20Cabinet.pdf?T=10

[2] Surrey's Climate Change Strategy, May 2020; https://www.surreyclimate.org.uk/sites/default/files/Surrey%27s%20Climate%20Change%20Strategy%20%28240420%29%20%281%29_0.pdf

[3] Greener Futures Climate Change Delivery Plan, January 2022; https://s3-eu-west-2.amazonaws.com/commonplace-customer-assets/surreysgreenerfuture/Final%20Climate%20Change%20Delivery%20Plan%20Full%20Document%202022.pdf

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