

The 'Split Ownership' model of shared ownership

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The most direct way that developers can meet the government's shared ownership expectations is to divide their scheme into sections and make part available for community ownership. We review the implications of this approach.

Executive summary

The 'split ownership' model, whereby an energy scheme is divided during the development phase into two substantially separate plants, one of which is to be owned and operated by a community enterprise; is the most fundamental approach to achieving the 'shared ownership' aspiration in the government's Community Energy Strategy.

The Shared Ownership Taskforce has assessed some of the specific issues, which this approach presents for the two eventual owners and their partners, and has made recommendations on how these might be addressed to make split ownership more widely applicable.

Several of these issues arise from the fact that the two primary partners become involved in the scheme at different times, yet wish to undertake final design and construction simultaneously for maximum efficiency and economies of scale. The differentials in expertise, resource levels and culture will also apply to this model as they will to other shared ownership approaches.

To alleviate issues identified, we specifically recommend that:

- DECC and Ofgem review Feed-in Tariff, Renewables Obligation and future incentive scheme registration processes to ensure that both plants in split ownership schemes can be accredited independently without problems;
- Distribution Network Operators are obliged to offer separate connection facilities, when called on to do so, to enable a community group to enter a split ownership scheme;
- The new Community Energy Association in England is given the resources to implement a platform where commercial developers can find suitable potential community partners;
- Peer mentoring programmes to accelerate knowledge transfer into new community energy groups are scaled up and adequately resources;
- The Green Investment Bank is enabled to provide funding to community energy groups to enable them to rapidly undertake the early stages of project development and 'catch up' with the commercial developer's timetable;
- Community enterprises are offered the same access to EIS-eligible funding for projects under the Renewables Obligation as they receive for projects under the Feed-in Tariffs; and
- Template contracts are developed to assist community groups engage rapidly in split ownership schemes.

What do we mean by split ownership?

The Taskforce is using the expression 'split ownership' to describe the approach where a scheme is divided into two or more separate generating systems, each of which can then produce energy for the benefit of an identified owner.

In the context of the Taskforce's terms of reference, it is anticipated that one of the eventual owners would be a community enterprise, in accordance with the government's community energy strategy. The other owner or owners would typically be the commercial project developer; or a utility, independent power producer, or investment fund to which the developer sells the energy generating station.

Although the principles in this annex apply to schemes which can be split into any number of sections, for any types of eventual owner, the remainder of the text will consider a scheme which is divided into two sections, one of which is retained by the commercial developer, and the other is taken over by a community group.

The split ownership concept is based on the premise that the scheme was initially conceived, or may otherwise have been developed, as a single system. The division of the scheme is undertaken to enable multiple owners to benefit from it, without entering a joint venture for the lifetime of the project.

It will often be uncertain, until later in the development process, whether there is a demand for partial community ownership. At the early stages, therefore, developers will tend to design the scheme in such a way that it can either be completed as a single station (we'll call this the 'single station option'), or divided into discrete plants.

Examples

There have been a handful of instances where wind farm developers have allocated a single turbine, or the output of a turbine, to a local community group.

Case study the Berwick-Cuckmere scheme

Potentially the first genuine split ownership scheme in the solar sector will be located near Berwick in East Sussex. The project developer Susenco recognised the benefits of working with the local community and considered from an early stage in the process the possibility of allocating part of an 8 MW solar park for community ownership.

A local community group was formed under the chairmanship of Dr Alister Scott and it has worked with the developers and landowners to enhance the ecological aspects of the proposed scheme and support the planning application. The proposed community involvement forms part of the planning consent.

A single connection approval was agreed with the distribution network operator UK Power Networks, but they later agreed to split the connection so that each plant has its own MPAN.

The developer identified prospective EPC contractors and ICPs on behalf of both the community project and the intended owner of the commercial plant, Low Carbon. They were therefore able to obtain economies of scale on the basis that both plants would be constructed at the same time using similar designs.

At the time of writing, the community group is incorporating as Cuckmere Community Solar Co-operative and contracts are being placed with the intention of building two neighbouring plants; a commercial station of approximately 7.5MW alongside the community plant of about 1MW. The community site is planned to incorporate extra ecological features and educational facilities.

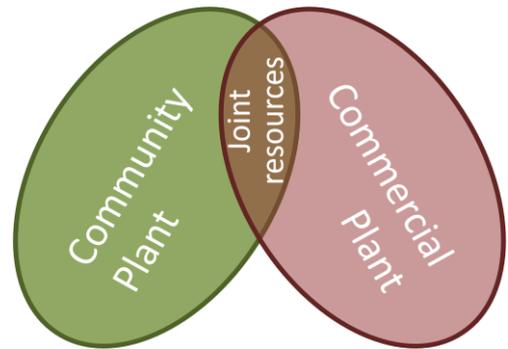
There may be potential in the future to extend the scheme by up to 4MW and it has been agreed that, if so, Cuckmere Community Solar would have the first option on this additional phase.



Degrees of separation

Because of the development process described above, there are likely to be some aspects which are common to both plants, while others are discrete and separate for each of them.

It is helpful to consider which aspects of the scheme might typically fall into the joint resources category.



Site and planning consent

We anticipate that it will be the norm for planning applications to cover the entire scheme and therefore the planning consent would typically be a joint resource.

The leasing agreements for the project sites are often agreed in outline at an early stage, typically as a single agreement. In many cases it will be preferable at a later stage to divide this into two discrete land leases. Alternatively it may remain as a joint resource, perhaps with a sub-lease for one of the plants.

Grid connection

Grid connection applications are typically made early in the development process, when the single station option still exists, and the initial connection offer is often therefore for a single point of access. It may be possible to divide this at a later stage into multiple connections each with its own Meter Point Administration Number (MPAN), failing which this will also remain a joint resource and arrangements will have to be made between the parties as further discussed below.

Capital equipment

The most common types of renewable energy systems are inherently modular.

Solar parks are made up of a large number of solar modules interconnected through multiple inverters. These can therefore be divided between different plants. In a wind farm, a defined number of turbines can likewise be allocated to each plant. One can envisage a similar approach for tidal stream turbines and wave generators, if the shared ownership approach were extended to these technologies.

Hydropower is less suited to split ownership, though a project incorporating multiple Archimedes screws, for example, could be divided in a similar way.

Combustion-based systems, including most types of bioenergy, seem less well adapted to this approach.

For electricity generation; power conditioning equipment, such as transformers and switchgear, can also be divided between separate sections of the plant. However, there is often a cost penalty for doing this and therefore some incentive to retain these elements within the joint resources as further discussed below.

Contractors

The primary contractors involved in building and operating the plant account for a substantial proportion of the project cost. These are the engineering procurement and construction contractor (EPC), the Independent Connections Provider (ICP), and the Operation and Maintenance (O&M) contractor. In principle all of these can be contracted separately for the two different plants. In practice, however, there would often be notable economies of scale in contracting with these jointly or, if separately, using the same contractors at the same time under substantially similar terms.

Similar principles apply to any secondary contractors such as asset managers, security providers, insurers, etc, but the economies of scale are probably less important and these arrangements may typically be contracted separately. Similar considerations will also apply to professional services such as legal and accounting.

Energy sales and incentives

If the separate plants are discrete as indicated in our definition, each will have its own arrangements for selling its output and registering for any incentive schemes. These issues are therefore unlikely to fall within the joint resources, although there may be benefits in collective negotiation with off-takers.

Issues with split ownership schemes

There are several factors which make a split ownership scheme more complex than an equivalent single development. We will firstly address the most significant factors before proposing some recommendations which would make split ownership a more widely adoptable approach.

Timing

Most such schemes are initiated by a commercial developer with the expertise, resources and funding in place (or at least with sources identified). The community partner is typically introduced at a later date and is much less likely to have the expertise, resources and funding required.

To avoid the inefficiency and expense of building the two installations separately, it is therefore necessary either for:

- (a) the community group to ramp up extremely fast; or
- (b) the development process to be delayed; or
- (c) the commercial project developer to finance the construction phase in the hope that the community group will be in a position to acquire it in the future.

None of these approaches is ideal for all those involved.

Risk

Both potential owners are to some extent dependent on the other for the efficient and timely completion of the project. This brings a degree of risk to both parties.

From the perspective of the commercial project there is a possibility that the timetable will be extended to accommodate the community group, as identified above. If, as is often the case, the community has not yet raised the necessary funding, there is the risk that it will not be able to complete, or take delivery of, its part of the scheme at the agreed time.

From the community's perspective, there is substantial reliance on the commercial partner to take the lead on technical aspects such as system design and equipment selection, and on contractual arrangements such as EPC and O&M contracts. In doing so, the community group may indeed be receiving the benefit of expertise which they could not provide on their own, but the net result might be one that is less appropriate for a community owned project.

Interdependence

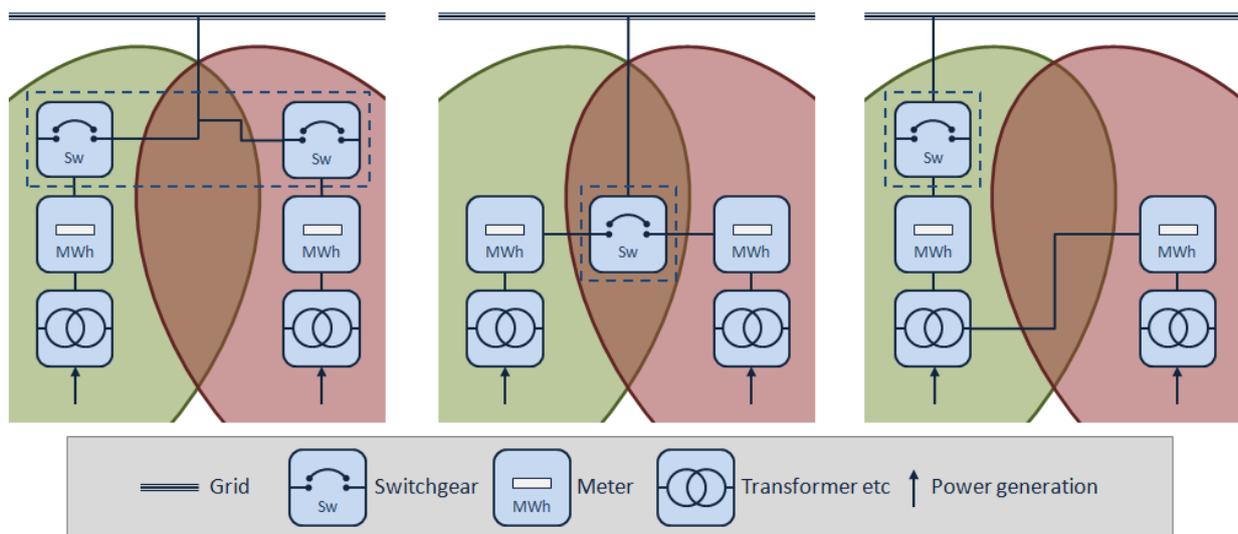
Another area of risk stems from the joint resources shared by the two projects. As discussed above; maximising the amount of such joint resource is likely to enhance the technical efficiency and cost-effectiveness of the overall scheme. Business and administrative drivers, by contrast, are likely to mitigate for the minimum level of overlap.

The commercial developer, for example, is likely to sell (or at least want to be able to sell) his plant on to some sort of financial institution. If there are aspects of its operation which are outside the sole control of the plant owner, this could lead to risks which make the proposition less attractive for the buyer. Reciprocally, the mutual owners of the community plant are at risk if aspects of its operation are dependent on the commercial project.

Interconnectivity

A specific instance of this issue is the way in which plants are connected to the export network. We discuss this in relation to connections to an electricity grid, but similar considerations could also apply to a heat network.

Different alternative connection and arrangements are illustrated below.



The option on the left has the lowest level of shared equipment. This is therefore more expensive because of the amount of duplication. It does however provide both owners with a high degree of independence from the other. It may be less susceptible to accreditation problems, as further described below.

The more integrated alternative in the centre has less duplication of equipment, so is likely to be more cost effective. However the two plants are more dependent on the shared equipment and connection.

The option on the right also avoids the need for a substantial amount of duplicated equipment. It makes the community plant highly dependent on the commercial one, in that the former is unable to export power to the grid if the latter's transformer or switchgear fails. Unless the commercial plant incorporates additional metering, it is dependent on the reading from the community plant to assess the output of the commercial station.

Dissimilar corporate structures

The entities owning the commercial and community projects are likely to have adopted different corporate and governance arrangements.

The community enterprise will typically not be a conventional for-profit organisation. In many cases these will be co-operative or community benefit societies governed by one member one vote irrespective of the size of investment.

Commercial organisations typically establish limited liability companies as special purpose vehicles (SPVs) to own each plant. These are normally private limited liability companies, in some cases

structured specifically to take advantage of enterprise investment scheme (EIS) or other tax advantages.

Although these differences do not create inherent problems, it can make negotiations between the participants more uncertain because of the different priorities and approaches that each brings.

Incentive measures

The UK currently operates two different incentive schemes for renewable projects, and is planning the implementation of a third. It is accepted that the Feed-in Tariffs (FiTs) are more appropriate for community projects, while the Renewables Obligation (RO) has been designed for larger commercial generators. The future Contracts for Differences are likely to be exceptionally onerous for community groups with limited energy market expertise.

The accreditation system for the Feed-in Tariffs in particular, and to a lesser extent the Renewables Obligation, has problems in recognising co-located or neighbouring plants. Ofgem's guidance for the Feed-in Tariffs has been developed specifically to prevent possible gaming by splitting up a large project into several smaller ones. As presently written, this would almost certainly prevent the commercial plant and the community plant being registered as two separate stations under the FiTs.

The regulations for the Renewables Obligation are (unhelpfully) rather different and would probably satisfactorily recognise a split ownership scheme as being two discrete plants provided that each has its own connection. However, it is unclear how Ofgem would deal with two neighbouring plants which shared a connection (one of the possibilities considered above).

It is anybody's guess how Ofgem will deal with a split scheme in which one plant is to be registered under the Feed-in Tariffs and the other under the Renewables Obligation (as proposed for Berwick-Cuckmere).

Differential fiscal, accounting and regulatory regimes

Successive governments have provided concessionary treatment for community enterprises to recognise the additional obstacles they face compared to their commercial counterparts, such as those described in this section. There are therefore several ways in which national fiscal and accounting policies differ for commercial and community organisations.

Accounting variations for community enterprises, compared to commercial companies, may include issues such as making returns to members through interest payments, rather than dividends; and the requirement to apply an 'asset lock'.

A specific instance of differential tax treatment is that EIS is available to community organisations earning income under the FiTs, but not to commercial companies. The government is introducing a similar exclusion from EIS for companies earning income under the Renewables Obligation. It is not yet clear whether an exclusion will be offered to community organisations as it was for the FiTs, but failure to do so would provide a further inconsistent market distortion.

The accreditation process for the Feed-in Tariffs also offers concessions to community organisations in that they have the right to seek pre-accreditation for projects from Ofgem. Under this procedure they may register a project and lock in a tariff level applicable even if the plant is completed and connected some months later.

Contractual arrangements

In principle a split ownership scheme is likely to generate twice as many contractual relationships as a single station, because each of the plants will probably require a full set of contracts with land-owners, developers, ICPs, EPC and O&M contractors etc. Furthermore legal agreements are likely

to be needed between the two eventual owners, covering any joint resources, inter-access arrangements and other matters.

In practice it may be possible to save a lot of duplication (of effort, if not paper) if the two owners aim, insofar as is possible to use mirrored contracts.

Recommendations

We set out below selected proposals, which could address some of the issues identified above and thereby make the Split Ownership model more widely applicable as a means of achieving the government's shared ownership aspirations.

Registration of split ownership schemes

Ofgem's Registration process for Feed-in Tariffs, the Renewables Obligation and similar mechanisms needs to recognise split ownership projects separately. It must not create barriers for the accreditation of either of the two power plants. This will require changes to the guidelines, and potentially even the secondary legislation, concerning the definition of a 'site' and a 'station'.

Action by: DECC and Ofgem

Split connections

To ensure that both plants can achieve the appropriate grid connection arrangements; distribution network operators should be required, on request from a split ownership scheme, to provide separate connections and MPAN's, even where the original connection offer was based on a single system.

Action by: DECC working group on community energy grid connections, Ofgem

Timetable synchronisation

The timing issues identified above can be ameliorated if support is given to help community enterprises move rapidly up the learning curve. Many of these issues will apply to other models beyond the split ownership approach.

Finding partners: A networking platform which helps commercial developers identify prospective community partners in their locations of interest would assist this process.

Action by: Community energy sector. The new Community Energy Association in England (CEE) is proposing to provide such a platform

Peer mentoring arrangements to help individuals in community groups to gain knowledge from those who have already successfully completed similar projects will also help accelerate the learning process. This should not be solely dependent on volunteers, but may also provide for reasonable payment to secure the services of suitably qualified mentors.

Action by: Community energy sector, Government. The Cabinet office has implemented a limited community energy peer mentoring program. Co-operatives UK plan to introduce a similar peer mentoring program shortly.

Early-stage funding

Community energy enterprises have proved successful in raising the capital to implement projects once they are reasonably well developed - i.e. consented and 'shovel ready'. The provision of funding at an earlier stage is more difficult; and this is precisely the time when the community groups will need to move fast to catch up with the commercial development timetable. New sources of funding will need to be provided, specifically tailored for this stage in the project and this level of risk.

Action by: Funding providers, Green Investment Bank, Government. The government's Rural Community Energy Fund and forthcoming Urban Community Energy Fund may be able to meet some of this requirement, but the application process will probably need to be accelerated if they are to do so. Pure Leapfrog and others are proposing to establish targeted funds specifically for this type of activity.

Fiscal incentives

The provision of incentives for community projects needs to be maintained and consistent. In the first instance this means that community enterprises should be able to take advantage of the Enterprise Investment Scheme when they undertake projects under the Renewables Obligation, as they can for Feed-in Tariff projects.

Action by: HM Treasury. A coherent case for this exemption has already been submitted to the Treasury.

Contractual standards

The provision of balanced template contracts to cover the likely aspects of the relationship between the two eventual plant owners would be of particular assistance to the community enterprises and would speed the process. Template contracts for other aspects would also be a useful resource (and could serve other models beyond the split ownership approach).

Action by: Service providers with community energy expertise. Some law firms have already been providing useful input to the sector, often on a pro bono basis.

Best practice guidelines

As soon as the first such schemes have been completed, the publication of a description of the split ownership model, together with guidance on how it can best be implemented would be a useful resource. A PR campaign to bring this to the attention of commercial developers would assist further.

Action by: Community energy sector

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