Melbourne Renewable Energy Project

The procurement process

This section provides information about how to navigate the procurement process, including market testing, cost modelling and tendering.

CNCA

The full guide is available here:
melbourne.vic.gov.au/mrep

CITY OF MELBOURNE

Most organisations have established ways of purchasing electricity, but this procurement process will be different. Most likely, it will require additional market scoping and engagement, more thorough due diligence – especially if a new facility is to be constructed – and new ways of structuring contracts. Work closely with your procurement team in the early stages to determine the process that will work best for you. Be prepared to be flexible, so you can test the market without locking yourself into a particular approach until you are ready.

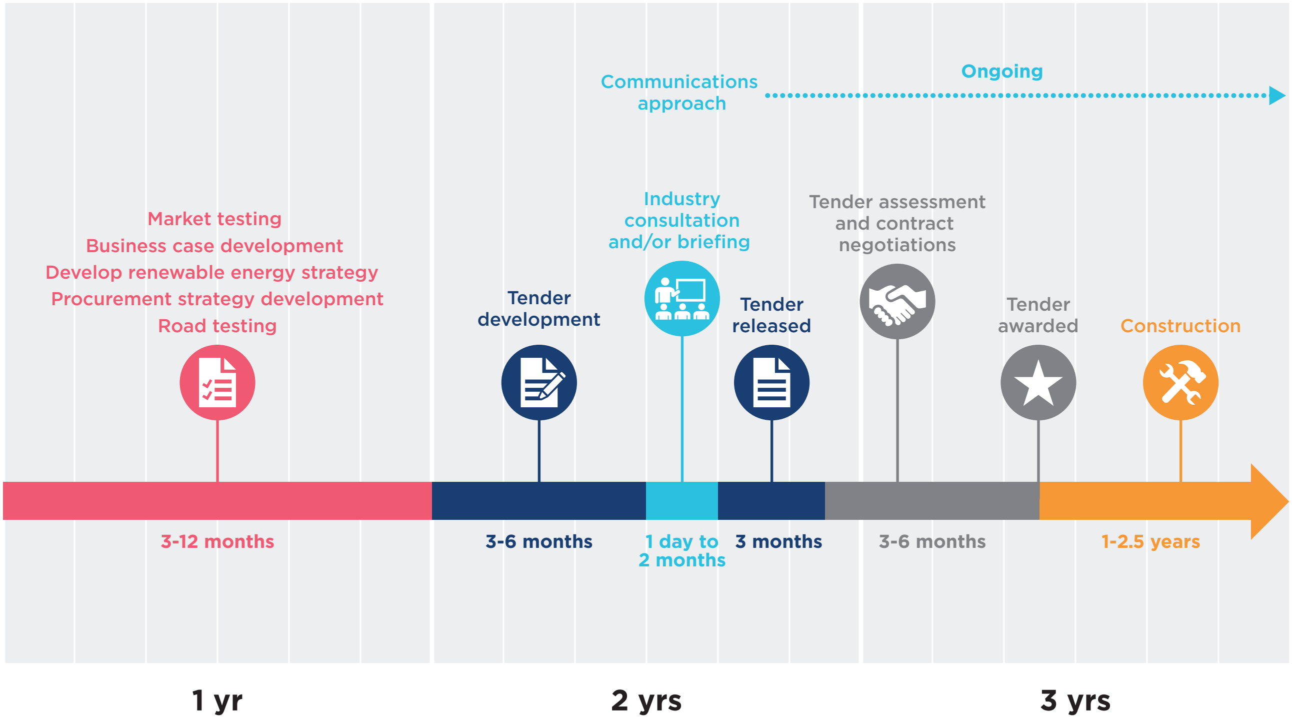
Key steps:

1. Test the market
2. Develop a procurement plan
3. Develop tender documentation and a tender plan
4. Develop contract documentation
5. Inform the industry, release the tender and conduct information sessions
6. Evaluate tenders and award

Timeframes might vary depending on the complexity of the tender and whether or not you are in a group. Buying LGCs from a broker is quite simple and straightforward, whereas developing contracts for difference and bundled contracts is more complex. The indicative timeline below shows a range of possibilities, from best case to blow outs.

> **TIP:**
> During project planning, map out the partner approval processes of all organisations to ensure you are creating adequate and realistic timelines. Partner approval processes vary depending on the type and size of the organisation.

Indicative Project Timeline



Market testing

The electricity market and the renewable energy sector are changing quickly. Before committing to spend considerable resources developing and executing a procurement process, it is prudent to test market conditions to determine whether a tender is viable.

Consider the following:

- the prevailing prices of electricity and certificates, and the federal and state government policies that affect them
- the availability of suppliers delivering the types of energy projects you are seeking
- attitudes of suppliers towards your favoured contract structure and length.

There are many ways to test the market.

- Seek expressions of interest. This could form the first step of an invitation-based tender.
- Speak with a number of known suppliers. This will help you develop your scope, but it may be less useful in getting a sense of pricing. (Be careful not to prejudice the outcome of an eventual procurement process.)
- Review published information about recently signed contracts.
- Review information published by Australian Renewable Energy Agency about projects in pre-development phase.
- Contact relevant state government departments to understand opportunities within your state.
- Assess recently announced government wind and solar auctions, if any.
- Contact regulators and industry bodies such as the Clean Energy Regulator and the Clean Energy Council.
- Speak with your energy advisor and with consultants who assist renewable energy developers.

MREP sought information from renewable energy projects, which were of sufficient scale to supply the group with its annual electricity needs. The request did not specify geography or technology. However, because MREP did not make a firm commitment to enter into a contract, respondents provided only overviews with broad pricing, rather than detailed proposals. The market has shifted significantly since testing was undertaken, but the results indicated that solar energy was cheaper in Queensland than in Victoria and wind was cheaper than solar overall. Biomass was more expensive than other technologies. The market testing indicated that there were sufficient projects to meet the group's requirements. It also provided the group with an understanding of long-term contract pricing compared with business as usual. On this basis the group decided to proceed to tender.

Competition law

The Consumer and Competition Act promotes fair trading and competition and prohibits anti-competitive practices. Provisions prohibiting collusive behaviour apply to suppliers as well as customers. Depending on the situation, there is potential for the purchasing group to breach provisions regarding agreements that contain a cartel provision, or may have the effect of substantially lessening competition within the meaning of section 45 of the Act.

The Australian Consumer and Competition Commission (ACCC) can 'authorise' businesses to engage in certain anti-competitive arrangements or conduct when it is satisfied that the public benefit outweighs the public detriment, including from any lessening of competition. An authorisation enables the group to undertake the purchasing activity, even if that activity would otherwise have been in breach of the Act. You can seek legal advice about these provisions and determine whether you need to apply for authorisation.

The organisations involved in MREP decided to seek authorisation from the ACCC to establish a joint electricity purchasing group, and jointly negotiate electricity supply agreements. The process took four months to complete (but it can be expected to take about six months). The ACCC determined that there were public benefits in reducing transaction costs and achieving economies of scale, as well as reducing greenhouse gas emissions and potentially increasing competition for retail supply of renewable electricity. It granted the authorisation for a period of fifteen years.[20] The ACCC does not make a determination about whether the purchasing group would contravene the Act – that would be a matter for the courts. Bear in mind that many purchasing groups choose not to seek authorisation, but seek your own legal advice.

20 You can download the authorisation on the ACCC website: www.registers.accc.gov.au/content/index.phtml/itemId/1194790/fromItemId/401858

Develop a procurement plan

Your procurement plan will need to meet your organisation's corporate rules and procurement requirements. While the process doesn't need to be led by a specialist, it is recommended that you engage a procurement advisor to help you plan. This may be an internal advisor or external advisor. Be prepared to challenge the established way of doing things. For example, it can prove useful to involve senior project team members who do not have a procurement background. Remember, this purchasing approach is unusual, so the procurement process may need to accommodate that.

The procurement plan will define roles and steps, and ensure that the process is fair, robust and defensible. It may include information about:

- purpose
- key deliverables
- key performance indicators
- budget information
- roles and responsibilities
- engagement with experts
- contract requirements
- market assessment
- procurement strategy
- probity and tender evaluation strategies
- procurement schedule
- risk assessment.

TIP:

Consider any procurement restrictions as soon as you can. If you are partnering with other organisations, check whether their procurement requirements and processes are different to your own and whether both can be accommodated.

Develop a tender

Corporate PPAs are a new and emerging area in Australia. Most suppliers will be engaging with this emerging market for the first or second time, and there will be a lot of uncertainty on both sides.

Work with your energy market advisors, procurement team and lawyers to develop the tender documentation – when you're done, have it reviewed by external advisors.

The tender may include several parts:

- conditions of tendering
- specification (such as NEM connection, new or existing project, construction timeframe, planning approval and technology type)
- evaluation process and criteria
- eligibility criteria, including corporate social responsibility and credentials of the energy producer and retailer
- description of contracting model
- schedules for respondents to complete, which may include: planning approvals, price schedule, community engagement plan, referees, capability and experience, stakeholder consultation, economic development, and marketing and communication specifications.

TIP:

If you are a purchasing in group, standardise members' requirements in the tender specification – that is, don't include different requirements for different customers. This will avoid the need to manage variable demands from stakeholders, and make it simpler to communicate tender needs to the market. It will also make it easier to evaluate and develop the final contract.

Tender evaluation process

The documentation needs to explain to prospective tenderers how their responses will be evaluated. Set out an evaluation plan detailing the process: how a decision will be made, how evaluation will take place and how scores will be determined. The full evaluation plan may not be included in the tender, but the two documents must be consistent.

As you determine weightings for scoring, bear in mind that some criteria – such as development risk, supplier capabilities and track record, and customer service and relationships – may need to carry greater weight that they would in a normal tender.

Tender evaluation weightings

MREP established five criteria for assessing tender responses. The most important was price (including the cost of contract management and price certainty), which was assigned 60 per cent of the weighting. Community and environmental benefits were assigned 12.5 per cent, retailer service and project delivery risk were both assigned 10 per cent. Finally, Victorian local community economic and promotional benefits were weighted at 7.5 per cent.

In 2014, the Australian Capital Territory released a request for proposals for wind energy for its large-scale feed-in tariff scheme. It stated that successful proponents would be awarded a feed-in tariff on a value for money basis (in dollars per MWh). In addition, it provided the following evaluation weightings:

- risks to timely project completion – 50 per cent
- local community engagement – 20 per cent
- ACT economic development benefits – 20 per cent
- reliance on treasury financial guarantee – 10 per cent.

Developing renewable energy projects is complex. It is likely that the evaluation panel will need to clarify issues and seek clarifying information from respondents. Depending on the scale and particular requirements of your tender, you could receive few or many responses. The tender result could be compromised if you need to exclude responses on the basis of unclear or insufficient information. Consider allowing for a two-step process in your procurement plan if you receive too many responses.

Try to establish an approach that will give you the information you require, while being fair to all participants and meeting your organisation's procurement needs. Given the scale and complexity involved, consider creating a special process outside your standard procurement process, and have it approved by your senior executive. Consult with your procurement team and probity advisor. You are likely to require specialist advice from external experts in undertaking the evaluation. Make sure that your procurement plan allows for this.

Develop contract documentation

Preparing contracts takes a lot of time, resources and costs, and requires specialist legal input. You can prepare draft contracts either before issuing a tender document, or after a preferred tenderer has been selected. There are pros and cons to each approach.

By drafting contract documentation before releasing a tender, you can clearly articulate your desired contractual outcome and provide clarity to respondents. This helps when it comes to developing the final contracts, because tenderers will have responded to something specific. However, the process is also costly for respondents, so they may not seriously engage with a draft contract until they have been shortlisted as a preferred supplier. At that stage, contract negotiations may result in significant changes to the contracts anyway. There is a risk that the initial contracts may need to be set aside for new documents, after the tender is run and terms are negotiated.

Instead of developing a fully formed draft contract, you could develop a term sheet, which identifies the key contractual points that the customer wishes to incorporate into a final contract. This approach may be quicker and less costly to both parties.

Another option is to develop term sheets and contracts after the tender has been run and a preferred tenderer, or shortlist of tenderers, have been selected. This approach requires robust tender specification, which clearly set out the expected terms of sale. By doing it this way, you will defer the cost of developing contracts until the nature of the contractual arrangement is better understood. This arrangement may suit a procurement process where your specification is less prescriptive and you are open to a range of purchasing options; for example, if you haven't decided whether or not to purchase LGCs, or to enter into a contract for difference arrangement and you intend to decide after evaluating the proposals.

TIP:

Lawyers and energy market consultants' time is valuable – and expensive. It may seem natural to contain costs by limiting their communication with one another, but the resulting delays and miscommunications may result in a more lengthy and costly process in the long run. Ensure that your consultants are communicating effectively and are involved when developing contract terms and documents.

As you develop contract documentation, one critical issue is 'bankability' – the financier must be prepared to lend to the project based on the terms that are agreed. Financiers, and therefore, project developers, will be particularly interested in supplier and customer termination clauses, the firmness of load over the long term, liabilities in case of default, and force majeure events (events beyond anyone's control). Meanwhile, you – and any partners – will be seeking a degree of flexibility to match your business needs, reasonable remedy provisions, and contract termination provisions in the case of under-performance or failure to supply, as well as measures to ensure that service standards are met.

The project will be more attractive for financiers if they can transfer some of their lending risk to the customers, by way of credit support. Under this arrangement, customers agree to underwrite some of the risk, should the retailer fail. The financier may also seek 'take or pay' obligations meaning that you would pay for the agreed volume of electricity or LGCs even if you fail to consume the agreed volume. It is common in energy contracts for a customer to have a right to vary their contracted load year to year by an agreed margin, usually 20 per cent. Instead of take or pay provisions, your supplier may agree to a charge for excess or under-consumption, based on a predetermined formula. There may also be other contractual solutions for managing the variability in your load that you could negotiate with your supplier.

Releasing the tender

To make sure potential suppliers are prepared and adequately resourced to respond, it is wise to signal to the market your intent to undertake a tender well in advance.

Electricity suppliers have limited resources and responding to a tender can cost thousands of dollars. When there are several tenders in the market, suppliers may choose to respond to the largest tender, or to the tender that seems simplest, or best suited to their business models.

You can signal intent to tender in the form of public announcement through industry publications or peak bodies such as the Clean Energy Council. Indicate in broad terms the size of the electrical and LGC demand, any generation technologies that are included or excluded from the specification, the contracting model you have selected and the term of the contract.

TIP:

Make sure the tender is open for a minimum of two months, to allow enough time for complete responses. If the tender is especially complex, consider allowing a longer period of time. Be aware of other tenders or project opportunities in the market that may compete with yours.

When you release the tender, you can offer information by holding public sessions or corresponding with interested parties. Be clear about what projects will and won't qualify. Be careful that any communications with industry conform with your procurement plan and are approved by your procurement team or probity advisor.

The MREP contract and pricing model was innovative and hadn't been tested in the market previously. As a consequence, suppliers found the contract structure challenging to understand. This resulted in considerable delay to the negotiation and development of final contracts.

LESSON: Spend time on market engagement before you issue the tender. This will simplify the process of developing and negotiating final contracts.

Evaluation, negotiation and award

You will need to form an evaluation panel, which may include outside experts, depending on your in-house knowledge and skills. The panel will require a Chair, who may be non-voting, and a secretariat to assist with managing documentation. Depending on your organisation, a probity advisor may need to attend meetings. Your lawyers don't need to be part of the panel, but you will need to call on them for advice and to negotiate on terms.

The panel is also likely to need support from energy market specialists to undertake a price review, technical due diligence and support you in the negotiation of the PPA. If you are taking an equity interest in the plant, you will need to undertake due diligence by specialists with experience in renewable energy construction and development.

TIP:

If you are purchasing as a group, your evaluation team and negotiating team may need to reflect the composition, needs and interests of the group. You may be able to draw on knowledge and skills from your partner organisations. But the evaluation and negotiation process will need to be confidential. Consider how you will seek input from your partners when negotiating without compromising confidentiality.

TIP:

Allow two months or more for the tender review and negotiation period. You need enough time to review the tenders, report back to project partners and undertake any necessary negotiations.

Evaluation, negotiation and award

Evaluation

Receive documents
- Determine eligibility for evaluation
- Request advice where necessary on issues, such as development risk

Develop preliminary scoring
- Determine which areas, if any, require clarification through interviews.
- Schedule interviews and presentations (if deemed necessary)
- Obtain clarifications where required

Negotiation

Develop final scoring
- Shortlist preferred tenderers
- Identify points that may need to be negotiated.
- Determine negotiating team. The negotiating team may need to be tailored to comprise individuals who have knowledge or skills relating to the issues being negotiated
- Undertake negotiations

Award

Final scoring
- Evaluation team complete final scoring and make a recommendation on a preferred tenderer

The full guide is available here:
melbourne.vic.gov.au/mrep