

APPENDIX 2 Update Paper for Partner Authorities:

Recent Progress on the Green Deal Finance Company and Potential Investment Opportunities for Partner Authorities

A. PREFERRED APPROACH (GDFC)

Update on GDFC

The Green Deal Finance Company (GDFC) is an industry led vehicle with the specific purpose of providing low cost finance for Green Deal loans. Its members include the big 6 energy companies, housing providers, building contractors, banks and also local authorities, including Newcastle City Council (NCC) on behalf of Warm up North.

The GDFC is to be funded from a mixture of junior and senior debt sources, with a target blended APR of 6.96%. The junior debt will be provided by DECC and the members of the GDFC, and will sit below the investment by the GIB, senior debt providers and the bond market.

In December the GDFC's first attempt to raise the junior capital (made up of high yield stakeholder finance and junior equity) was unsuccessful. The main reason for this was mixed responses from the 'Big 6' energy companies.

The GDFC has subsequently made the following changes to its terms to incentivise the energy companies and Green Deal providers to invest at the required levels:

- No Green Deal Provider can access the GDFC if they haven't provided stakeholder finance
- No Energy Company can use Green deal loans funded through the GDFC to discharge its ECO obligations if they haven't provided stakeholder finance

On this basis a second call for junior capital was issued in January, along with higher investment from DECC and PwC, and this time an appropriate amount of finance has been raised.

In parallel, the systems required by the GDFC, mainly relating to IT interfaces and loan administration, have been successfully procured and will go live in line with the target timescale.

On the basis of these developments the stakeholder loan agreement will be signed on the 1st February with a number of conditions precedent, the main ones relating to due diligence and state aid clearance from the European Commission (State Aid clearance from the Commission is expected on 5 February).

All this means that we can have greater certainty that the Warm Up North project will be able to draw finance from the GDFC than at any other time in the procurement.

Partner Authority Lending Opportunities

As per the above, the GDFC has now secured the required amount of stakeholder funding. This will likely include a modest symbolic contribution from Newcastle. The GDFC will still need additional junior capital to sit below the GIB and senior debt.

The Junior Capital element will directly fund improvements to households, and will therefore be classified as a loan for capital purposes. NCC's main issue with providing funding at this level is that the investment will need to be ring-fenced for use within the authority boundary, and all Partner Authorities would probably require this.

To facilitate this, Manchester have come up with a proposal where investment is staggered, so that further investment only takes place once an initial sum has been demonstrably invested within the Greater Manchester area two or three times over. This will ensure that the funding is delivering local improvements, and also that it is leveraging in further finance.

Local authorities may not be under any obligation to provide junior capital to utilise the GDFC, but doing so will ensure the availability of GDFC finance in their region. In addition the funding is anticipated to generate returns of 10%. NCC are not minded to make any investment prior to having a WuN preferred bidder, which is programmed for Summer 2013.

B. RESERVE APPROACH (Prudential Borrowing)

Whilst the progress the GDFC has made in recent weeks is significant and encouraging, there are still a number of risks over its ability to fund all WuN Green Deals over the 5 year projected programme. These include:

- State Aid (though formal clearance is expected on 5 February)
- The GDFC's ability to secure senior debt, and sufficient interest from the bond market
- Sufficient national demand to sustain the GDFC
- Snagging issues with systems, resulting in delays

For these reasons, the Partner Authorities will continue to commit to provide a reserve approach, either on a short or long-term basis, to give the short-listed bidders sufficient confidence to bid for the project. Bidders will be asked to comment on proposals for the reserve approach through dialogue and in their final tender submissions.

The Partner Authorities committed to provide funding for Green Deals if required in the MoU, and this obligation is included in the first draft of the Inter Authority Agreement, which is now with Partner Authorities.