Module structure

The Community and Renewable Energy Scheme (CARES) Toolkit is intended to be used as a reference by community groups of all kinds. This module is one part of a series of documents forming the CARES Toolkit and is designed to cover all sizes of project, although the scale and complexity of multi-MW projects may require more detailed evaluation than smaller projects. Other modules that may also be of particular interest to those reading this module are as follows.

- Establishing a community group
- Project finance
- Securing the site
- Planning
- Grid connection

This module has been developed for Local Energy Scotland to provide support to community groups looking to invest in a renewable project that is being developed by a commercial developer. The module outlines the different factors that need to be considered when making an investment decision and how to obtain the relevant support when making these investment decisions.

It is part of the CARES Toolkit and in addition to this module, there are other relevant guidance documents and tools available that should be reviewed in conjunction with the following modules:

- **Project Finance module** – this module provides an overview of renewable project finance, the terms that are used and how to determine the financial viability of a project.
- **Sources of Finance** – this module lists some of the available sources of finance for a community group looking to invest in a commercial project. This includes grants and loans from traditional financiers and more innovative sources of finance.
- Finance Glossary – a summary of the finance terms used in renewable projects.

Background

Shared ownership in renewable projects is commonplace across other European countries. Denmark has a long history of community owned renewables[1]. In the 1980s and 1990s the majority of wind turbines in Denmark were owned by locally owned co-operatives. Co-operatives that were set up to fund, develop and construct local renewable projects.

The Middelgrunden co-operative in Denmark operates 50MW of renewable energy generation. In 1997, the Danish island of Samso[2] set about a switch to renewable energy sources and 8 years later, started generating 100% of its energy needs from renewable sources for its' 4,000 inhabitants.

The co-operative approach in Denmark has been at the core of the Danish wind industry. Danish government policy works to encourage significant financial participation and co-ownership from landowners and locals. Developers were required to offer up to a minimum of 20% of shares in a project to individual householders living within a 4.5km radius of the site. Shares not taken up are then offered to other householders in the wider municipality.

In Germany, public engagement in renewables has raised €30bn of household and shared ownership in renewable energy schemes, unlocking a significant source of finance[3]. In 2012, Germany reached 72,907MW installed capacity of renewable energy; 25,049MW of which a third (34%) is considered to be community owned[4].

There are many models that allow shared ownership of a renewable project. These include:

- **Owner operator** – project development and construction is led by the community and funded by the community, with the community operating the project.
- **Commercial developer led** – project development and construction is led by a commercial developer, with the community being offered an investment stake in the shared ownership project or even full ownership.
- **Community developer led** – project development is led by the community and a developer is approached to construct and invest in the shared ownership project.
- **Joint ventures** – where a commercial operator and legally-constituted community organisation work together to create a joint venture to develop, own and manage a project.
- **Shared revenue** – in which a legally-constituted community organisation buys the rights to a future virtual revenue stream which will be calculated on the basis of a specified proportion of the output of an installation, less agreed operating costs and generally less virtual debt service. This is calculated as if the community had acquired the underlying infrastructure.
- **Split ownership** – in which a legally-constituted community organisation owns a proportion of a development's physical assets, for example, the community

[1] Community Power - Denmark
[2] Community Power: the benefits of an energy revolution
[3] DECC Community Energy Call for evidence 06/06/2013
[4] Community Power - Germany

organisation owns one wind turbine in a development of 20 turbines being installed by a commercial developer.

The owner operator model is explored in considerable detail in the project development section of the CARES Toolkit. The focus of this module are the other models for a community to invest in a project.

Historically in the UK, financial institutions have appeared to be less willing to lend to smaller renewable projects in comparison to Denmark and Germany. This is in part due to the high fixed costs in arranging finance which therefore favours larger projects requiring larger investments. To date, this has left community-based developers relatively dependent on government loans and support mechanisms for a proportion of capital costs, which can prove difficult and time-consuming to obtain.

However, as outlined in the Sources of finance module, there are ever increasing sources of finance available to communities looking to develop their own project or invest in a commercial developer led project.

The Scottish Government's target is to generate of 100% of Scotland's gross annual electricity consumption with renewables by 2020. The Scottish Government believes that communities can contribute to this target by delivering 500MW of locally owned renewable energy. There are a number of enabling factors that the Scottish Government has put in place to help deliver this target, one of which includes the recent Scottish Government Good Practice Principles.

CARES has an important part to play both in supporting communities in the development of locally owned projects and in the opportunities that are available to invest in renewable projects being developed by others further afield.

Shared ownership models

The following are examples of how some shared ownership models may work in practice.

Shared Ownership structures: JV 1 where each party contributes a percentage of the investment costs and owns part of the assets

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Legal ownership	Joint venture company				
Shareholders	Community	Community	Private developer	Private developer	Private developer
Development phase risk	Normally with the private developer who may charge the JV a development fee, which the community will need to negotiate to ensure it is still making suitable returns. The question is when does the community start engaging				
Equity funding	Community	Community	Private developer	Private developer	Private developer
Debt funding	Community finds *	Community finds *	Private developer finds or could finance from own resources (on balance sheet)	Private developer finds or could finance from own resources (on balance sheet)	Private developer finds or could finance from own resources (on balance sheet)
Maintenance and operations	With the JV (normally arranged by private developer), which the community will need to negotiate to ensure the costs are reasonable				
Profits to each party	20% of wind from 1, 2, 3, 4 & 5 to community	20% of wind from 1, 2, 3, 4 & 5 to community	20% of wind from 1, 2, 3, 4 & 5 to private developer	20% of wind from 1, 2, 3, 4 & 5 to private developer	20% of wind from 1, 2, 3, 4 & 5 to private developer

* Problem is unless the private developers and the community have the same bank then no commercial bank is likely to lend to the community as loan cannot be secured against assets. This means the community may need to find softer debt finance (e.g. REIF or a Crowd Funder) that may be prepared to lend

1 Ricardo-AEA in Confidence © Ricardo-AEA Ltd

Shared Ownership structures: JV2 where each party contributes a percentage of the equity and owns part of asset, but JV secures debt

RICARDO-AEA

	 1	 2	 3	 4	 5
Legal ownership	Joint venture company				
Shareholders	Community	Community	Private developer	Private developer	Private developer
Development phase risk	Normally with the private developer who may charge the JV a development fee, which the community will need to negotiate to ensure it is still making suitable returns. The question is when does the community start engaging				
Equity funding	Community	Community	Private developer	Private developer	Private developer
Debt funding	JV finds one debt financier				
Maintenance and operations	With the JV (normally arranged by private developer), which the community will need to negotiate to ensure the costs are reasonable				
Profits to each party	20% of wind from 1, 2, 3, 4 & 5 to community	20% of wind from 1, 2, 3, 4 & 5 to community	20% of wind from 1, 2, 3, 4 & 5 to private developer	20% of wind from 1, 2, 3, 4 & 5 to private developer	20% of wind from 1, 2, 3, 4 & 5 to private developer

Shared Revenue: Basically the same as JV 1 except even harder to secure debt as community owns no assets

RICARDO-AEA

	1 	2 	3 	4 	5 
Legal ownership	Private SPV company (Special Purpose Vehicle)				
Shareholders	Community	Community	Private developer	Private developer	Private developer
Development phase risk	Normally with the private developer who may charge the SPV a development fee, which the community will need to negotiate to ensure it is still making suitable returns				
Equity funding	Community	Community	Private developer	Private developer	Private developer
Debt funding	Community finds *	Community finds *	Private developer finds or could finance from own resources (on balance sheet)	Private developer finds or could finance from own resources (on balance sheet)	Private developer finds or could finance from own resources (on balance sheet)
Maintenance and operations	With the SPV (normally arranged by private developer), which the community will need to negotiate to ensure the costs are reasonable				
Profits to each party	20% of wind from 1, 2, 3, 4 & 5 to community	20% of wind from 1, 2, 3, 4 & 5 to community	20% of wind from 1, 2, 3, 4 & 5 to private developer	20% of wind from 1, 2, 3, 4 & 5 to private developer	20% of wind from 1, 2, 3, 4 &5 to private developer

* As the community do not own any of the assets it is unlikely a bank will be prepared to lend money to the community. This means the community may need to find softer debt finance (e.g. REIF or a Crowd Funder) that may be prepared to lend

Split ownership

RICARDO-AEA

	1 	2 	3 	4 	5 
Legal ownership	Community ownership		Private company		
Shareholders	Community	Community	Private developer	Private developer	Private developer
Development phase risk	Either on own, or private developer who may charge the community a development fee, which the community will need to negotiate to ensure it is still making suitable returns. The question is when does the community start engaging		Either on own, or private developer who may charge the private company a development fee.		
Equity funding	Community	Community	Private developer	Private developer	Private developer
Debt funding	Community		Private developer		
Maintenance and operations	On own or deal with private company		Private company		
Profits to each party	50% wind from 1 & 2 community	50% wind from 1 & 2 community	33.33% of wind from 3, 4 & 5 to private developer	33.33% of wind from 3, 4 & 5 to private developer	33.33% of wind from 3, 4 &5 to private developer

CARES support

CARES provides assistance to support communities in the uptake of renewable energy projects, either as developers of their own projects or investors in projects led by commercial developers.

If you are considering investing in a renewable project, the following support is available to you through CARES:

- **CARES enablement grants –** funding is available to fund non-capital aspects of a project and can help with start-up costs of feasibility studies, community consultations and other preparatory costs.
- **CARES development loans/grants** can be used for development costs in a shared ownership project.
- **Guidance from local development officers** – local development officers are located around Scotland and have local knowledge of the factors influencing renewable energy projects in their areas.
- **CARES Project Finance Model** – This can be used to provide an indication of the financial performance of a renewable energy project
- **CARES Investment Ready Tool –** a tool to prepare your project for approaching potential lenders.
- **CARES Procurement module** – a guidance module is available to support the procurement of professional services that will be required when making an investment decision. This includes template Invitation to Tenders for procuring services.
- **Shared Ownership Opportunities guidance –** additional information on shared ownership of projects.

Benefits of investing

Figure 1 shows the increased financial benefit that a community group might expect to realise from greater involvement in a community renewable project. A community that realises community benefit payments from a commercially led project can expect to receive up to approximately £5,000/MW of installed capacity per annum.

The Scottish Government's Register of Community Benefits provides an indication of the level of benefit payments other community groups have received. With limited involvement from the local community, there is limited risk to the community.

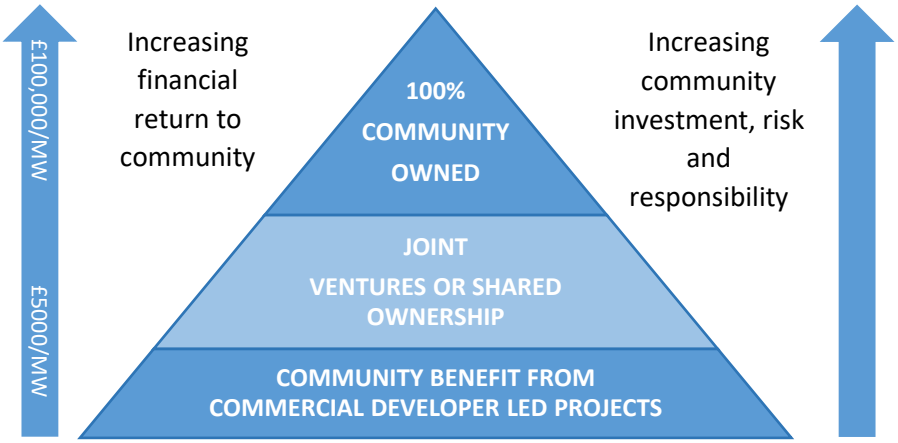

Figure 1 - Risk and effort verses reward chart

At the other end of the scale is a project that is community owned and developed. The financial benefits to the community are significantly greater, as are the risks and responsibilities. More benefit is achieved if investment in the project is early, however, this has more associated risk. Returns of up to £100,000/MW per annum have been realised by some communities. It is also important to note that investments have to be committed for 20+ years for some technologies, regardless of whether it is a commercial developer or a community led project.

In shared ownership opportunities, there are many case studies of the commercial developer leading the project and taking the development risk. Subsequently, the community is offered an opportunity to invest. There are no set criteria for the terms of the investment or the relationship between community and developer, with each project being unique, so each project should be evaluated individually on its own merits. Professional advice is recommended before making any investment decisions.

There are more benefits to the community and the commercial developer to be realised from this shared ownership approach than simple financial benefits. The Scottish Government's Climate Change Plan suggests community involvement in generating electricity, whether fully community-owned projects or part community ownership of larger commercial projects, can help achieve our goals of decarbonising the power sector. With a target of 2GW of community and locally owned energy by 2030.

It is often claimed that "projects are more likely to succeed if they have broad support and the consent of local communities"[5]. Further research into planning rejection rates has confirmed that the impact of community involvement is significant in certain local authorities, although not all local authorities[6]. If a community were to invest in a project before a planning application is submitted by a commercial developer, there is potential to increase benefits, but at the same time this approach has greater associated risks. Opportunities for

[5] UK Renewable Energy Roadmap - 2011
[6] ResPublica: The Community Renewables Economy - 2013

potential investments can be identified by approaching local landowners or reviewing local authority planning applications.

An estimated 697 MW of community and locally owned renewable energy capacity was operational in Scotland in 2019 from a mixture of solar PV, onshore wind, and hydro projects. This is a 6% increase on the operational capacity in June 2017.

The operating capacity resulted from a total of around 18,830 individual renewable energy installations.

Professional advice

There are many rules and regulations governing the financial market and how investment deals are managed. This includes what types of organisation are able to make commercial investments. As a result, it is important to seek professional guidance early when making commercial investment decisions.

Most projects are likely to require advice from specialists such as lawyers, solicitors, accountants, and other technical specialists. The community must lead the project but assistance from others should be considered. This will reduce the project risks as specialists will bring experience and knowledge to the team. The Establishing a community group module provides further information on the skills required when developing a project. From this, it is possible to determine which skills are available within the group and which should be procured.

The following list describes the support that may be acquired from financial and legal specialists when considering an investment in a renewable project. The CARES enablement grant can be used to procure these services.

Local Energy Scotland set up a framework of legal and financial advisors who could offer additional support through CARES. For further information you can contact your local development officer.

Before approaching a professional advisor it's important that you are clear about your aims and goals for the project you are exploring. This will be useful in the early exploratory discussions with the advisors. Ask yourself the following questions:

- What outcomes are you hoping to achieve? For example, is it financial security for the community? Is it energy security? Is it revenue generation?
- What is the nature of the undertaking in the project? For example, is it a joint venture? Is it a shared ownership investment opportunity?
- What are your key drivers? For example, are the reducing carbon emissions? Community development? Long term community sustainability?
- What is your appetite for risk?
- What level of involvement do you want in the project? For example, as an investor, operator, or developer?

- What level of investment are you considering? Do you have equity to invest? Would you be raising debt finance?

Financial specialists

- **Financial Modelling –** This is required to determine the financial feasibility of project. This service will also help to determine the potential financial benefits for the community
- **Transaction support** – The specialist provides advice or acts as facilitator on behalf of the community to attain their financial requirements. The services to consider here include:
    - Preparation of financial and business plans
    - Identification of potential sources of finance or developers
    - Lead debt and equity raising
    - Review funding structures, returns and ability to make the payments on debt
    - Lead negotiations with commercial developers
    - Permitted value gain study.

- **Strategic Advisory** – This service helps bridge the gap between the method to attain finance, attaining the finance and then paying the debt. The likely services provided under this would include:
    - Provision of an Independent Financial Conduct Authority Approved Financial Adviser
    - Advice on strategic options and ongoing review of business plans and financial forecasts
- **Social Impacts Services –** This is where economists ascertain the non-financial benefits of the project. The service can then determine how they could benefit the project. The services here can include:
    - Economic benefit analysis
    - Cost saving analysis
    - Alternative sourcing
    - Social impact bonds.

Legal specialists

- **Due diligence and review of the commercial offering** – This is where all the legal documents for the project are considered. The aim is to ensure that from a legal perspective the community receives the greatest benefit.
- **Structure community group for investment –** This is an important requirement as there is likely to be significant legal requirements linked to the financing option. The likely areas covered here would be:
    - Negotiating and agreeing the legal documents related to the finance package; and
    - Considering and dealing with the formalities of completion.

  Some of the community group structures that may be appropriate are outlined in the Establishing a Community Group module.

- **Finalise negotiations with commercial developer** – This is where the legal team will check the documentation to ensure that they are acceptable. The likely services here will include:
    - Negotiation and agreeing legal documents are acceptable for the funding package; and
    - Consider all the various stakeholders and parties involved in the project and ensure all contractual requirements are covered.

The Procurement module includes guidance on procurement and template Invitations to Tender (ITT) which outline the services required. The ITTs provided are only examples and have to be tailored to meet the project requirements. Each project is likely to be unique, so some form of tailoring will be required.

As each project is different, their project path to completion will be different. This means that a community should always keep decisions open for as long as feasible. This is particularly true of investment decisions as they are likely to impact the investment structure which in turn is likely to impact finance availability.

The timeline for a project can be complex, therefore it is important that communities approach specialists at the right time. Early preliminary investment advice can assist the community in two ways:

1. Gain an insight into the general investment opportunity before full & detailed analysis is carried out, and time and money is spent; and
2. Ascertain whether there is a general appetite for the investment.

If receiving support from CARES, a community group will be required to produce a community development plan and complete community consultation. Further information on this is available in the Establishing a community group module.

How community projects are financed

Whether the project is community led with the community instigating and owning the project, or developer led with the community co-investing, there are only three sources of finance available for a community, notably:

- Debt Finance (eg a bank loan)
- Grants
- Equity.

These are explained below. Different providers of this finance are listed in the Sources of finance module.

Equity

The community may already have money from other sources it is investing on its own account, or there may be a few locals investing. This would be classed as equity. Equity

may be also be a share offer that a group uses to raise funds. If a share offer is through a co-operative, then the return on investment to members is limited to that which is sufficient to raise and retain the capital the co-operative islooking for. This means the co-op is not in business solely to make profit for investors but must also put some of their profit towards the objectives of the organisation. Further information on co-operatives is available in the Establishing a community group module.

Should a community have its own source of equity, this can be used to invest in the project. This might be a direct cash investment, or if the community owns a piece of land, they might take out a loan against the value of the land to invest in the project. That would tie up their equity as it has been invested elsewhere. This would not prevent the community from using the land, but it would prevent them from using the land to raise finance for other projects.

The Islay Energy Community Benefit Society [7]recently raised over £500,000 through a community share offer. In this case members of the community were being offered a stake in the community benefit society, the owners of a 330kW wind turbine, and will have shareholder voting rights in the community benefit society and direct control over the project.

Grants

Public sector grants are generally provided to projects to fund a particular service or activity. There will be a number of restrictions associated with the grant and how it is used. It is important to clearly understand the terms and conditions of the grant and under what conditions the funder may want the grant to be returned. If the project requires additional debt finance, lenders will want to fully understand the terms of the grant.

There are restrictions on the amount of grant funding a project is able to receive if it also wishes to receive renewable subsidies such as renewable obligation certificates (ROC). Ofgem has authority for confirming whether a project can receive both a grant and a government subsidy.

There are defined ‘permitted grants’ that a project can receive in addition toother renewable subsidies. A grant from public funds is a ‘permitted grant’ where the offer of the grant was accepted:

In respect of reasonable additional costs of an installation to avoid or mitigate environmental harm. In order to qualify, the amount of the grant must not exceed the amount of those identified costs.

Such additional costs may include, for example, measures to protect fish and other wildlife in small hydro schemes. Additional costs associated with land acquisition or inefficient or poorly located installations would not be reasonable additional expenditure.

[7] Islay Energy Community Benefit Company: An invitation to purchase shares

There are European Commission (EC) de minimis regulations that also govern the amount of grant funding and generation subsidy a project is able to receive. If the overall support to be received from public funds does not exceed thresholds specified in the de minimis regulations[8] the project may be eligible to receive FITs payments and retain the grant, provided all other eligibility criteria are met. Further information on the de minimis regulations is available on the UK government website.

Private grant funding, such as those that may be available via the community benefit payments from local renewable projects does not conflict with the EC state aid regulations.

Debt finance

Commonly the community will have few assets it can use as security for a loan, so banks and other lenders will provide ***non-recourse finance*** where the debt will be secured against the actual physical assets and the future cash flow stream from the renewable energy project. This is also called project finance. Therefore, in the unfortunate case where the project doesn't do as well as anticipated and the debt cannot be repaid, the lender can step in and take ownership of the asset and try to reclaim some of its monies. It is non-recourse debt as the lender cannot try to claim money from other projects the community may have.

Different lenders include:

- **CARES -** A CARES development loan can be used where a community group is looking to invest at an early stage, pre-submission of a planning application.
- **Commercial banks** – There are many commercial banks available who are interested in investing in renewable projects. Generally commercial banks will be looking for larger scale investments of more than £2.5million as the setup costs for loans any smaller than this makes the proposition less attractive. However, this does not exclude them from small investments.
- **The Charity Bank** – The Charity Bank provides loans to social enterprises and other community organisations that benefit people and communities.
- **Social Investment Scotland (SIS)** – SIS is a registered charity and social enterprise that provides business loans to third-sector organisations.
- **Scottish Investment Bank** – Community renewable energy projects that have successfully gained planning permission can apply for support from the Energy Investment Fund (EIF). EIF is delivered by the Scottish Investment Bank, on behalf of the Scottish Government.

Where there are a number of lenders to a project and the lenders are not co-lending on identical terms the lenders will have different rankings of seniority. For example, a commercial bank may assume the position of senior lender and the Scottish Investment Bank may assume the position of a junior lender. This is the ranking of the security that a

[8] In most cases this threshold is €200,000 over a period of three years

lender has in a project. In a worst-case scenario where the project fails, this is the order in which any outstanding value within the project is repaid to investors.

Community-led versus developer-led investment offerings

A community-led investment is easier to understand as the community will own the entire project. A developer led investment offering is more complicated as there are a number of different options the community may be offered. The project developer is using their experience and expertise to develop the project and offering the local community a stake in the project as a shared ownership.

This might be shares in a proportion of the project, with an estimated return on the investment. Alternatively, it might be a share of the whole project, including a proportion of debt required to finance the project. Or it might be a proportion of the income stream in return for a proportion of the final cost.

For the Neilston Community Windfarm (see Case Studies Section, below), the local development trust, Neilson Development Trust, partnered with a developer, Carbon Free Development and raised investment which allowed a 28.3% ownership in the project. The terms of the investment that was offered to the community were the same as the terms offered to the developer.

For a community group to invest in a project, they will be required to set up an appropriate shared ownership structure, a Community Vehicle. It is important to understand exactly what the offer is, as it influences the legal framework under which the community group would incorporate itself and the opportunities for raising finance. There are an increasing number of opportunities for communities to take an ownership stake in a project, where they are partnered with one of more of the stakeholders involved in the project. As a result there is an increasing diversity of Community Vehicles that enable this partnership. See Local Energy Scotland's shared ownership portal.

Where there are a number of stakeholders investing in the project, the size of the stake each will have will relate to the level of investment they will be required to make, and the level of control they will have over the development of the project. The offer to the community group may or may not allow voting rights in the project.

All of these factors can influence the sources of finance that is available to a community. For a full list of sources, please refer to the Sources of finance module. If a community share offer is made through a co-operative, then how the finance that is raised is used and invested in the project is controlled by the co-op members. It is up to the investors to determine whether they are happy to invest in a project in which they may or may not have voting rights. For this reason, professional advice, either from within the community group or external sources is important. It is important to have as much information available as possible before making any investment decision and to be clear on the implications of the investment.

Whatever the offering to the community, the community will have the same choice of three finance sources, although most developer led scenarios may preclude access to commercial bank loans.

If there is a shared ownership proposal being offered to a community, there may only be a short amount of time to find money, so use the CARES Project Finance Model as a start to see if it is worthwhile. Then start speaking to financiers. Once you have the full Investment Memorandum you can approach an FSA approved adviser to evaluate the investment in more detail.

The implications of being able to borrow money from commercial banks if the developer does not offer ownership of some of the assets are illustrated in the following four scenarios.

Developer raises money with non-recourse bank loan and other sources

In this case the developer may raise 70% or more of the project costs with a bank loan secured on the project assets being developed and the future cash flows of the project.

If the developer only grants access to income streams then a commercial bank is very unlikely to lend to the community group unless the commercial bank is the same as the developers own bank, in which case it may.

Developer raises money with recourse bank loan

Recourse finance are loans secured against some additional assets which are used as collateral. For example, if a developer owns a number of other renewable projects outright and does not have any outstanding finance against these projects, these could be used as additional collateral against which the developer can borrow money to finance other renewable energy projects.

If the developer only grants access to income streams then a commercial bank is very unlikely to lend to the community group, even if the same bank the developer is using is approached as the bank is lending on a recourse nature to the developer.

Developer uses existing money to finance the project

The developer may have a strong cash flow position and not even need to approach a bank. If the developer only grants access to income streams then a commercial bank is even more unlikely to lend to the community group as no other lender is involved.

Developer loans community finance

Developer can lend to the community group using the same resources as 6.2 and 6.3.

Venture capitalist finance

Venture capitalist finance is another potential source of finance to a developer. In this case, the project developer is looking to raise finance from a venture capitalist investor. There are a number of venture capitalist companies that can raise finance for a renewable project. For

example, there are Venture Capital Trusts (VCTs) and Enterprise Investment Schemes (EIS). The attraction of both VCTs and EIS is that they offer income tax relief.

It should be apparent that this is a complex area that again requires input from a professional financial adviser.

Like bank loans, venture capital finance also tends to be long-term, but often not as long as a bank loan. After a number of years (generally no more than 5) venture capitalist finance will look for a return on their investment and the developer will be expected to find an alternative source of finance to repay the original loan. At this stage the project will have a proven track record of annual energy production.

~~As with Section **Error! Reference source not found.**,~~ If the developer only grants access to income streams then a commercial bank is highly unlikely to lend to the community group as no other lender is involved.

Different legal structures for your group

To access any of these sources of finance it is a requirement that an incorporated structure is set up. This provides the Community Vehicle with the legal status required to issue shares, receive grants or secure loans. The Community Vehicle will also be able to enter into contracts and employ staff, which may be a requirement of entering a shared ownership agreement with a commercial developer.

The following structures may be suitable for your organisation:

- Registered society[9], which can be either be
    - Co-operative Societies (Co-ops), or
    - Community Benefit Societies (Bencoms).
- Community Interest Company (CICs).
- Private Company Limited by shares (CLSs).
- Private Companies Limited by guarantees (CLGs)
- Charitable Status.

Additional information can be found in the Establishing a community group module.

Community-led developments

If a community has identified a potential site for a renewable project to be developed they have a number of options to consider for the development of the project.

1. Community led development – the project development section of the toolkit provides further guidance on developing a site and raising finance
2. Community led development with third party support – organisations such as Energy4All exists to support communities in the financing and build of their

[9] Which were previously known as Industrial and Provident Society (IPS)

consented projects, allowing the community to retain control over the development of the project

3. Community led development with commercial developer support – having identified the project, a commercial developer is approached to develop the project further

There are benefits to all of these options. Community led developments, and those with third party support, ensure that the control of the project is maintained locally through the construction phase and beyond. By engaging a commercial developer, the project is likely to be developed more quickly and could require less input from the community. It is possible that the commercial developer will expect to retain control of the project.

For any project development, collating the information required within a business case is a useful first step. If taking a project further with support from a third party or a commercial developer, they will be interested in understanding the land ownership arrangements at the site and any similar projects that are in operation locally. The Securing a site module can provide further information on how to complete this. Before approaching the developer, if possible, an exclusivity agreement should be entered into with the landowner.

Business case

When taking a project to a potential lender or seeking support from a third party it is good practice to compile a business case which demonstrates and explains the benefits of completing the project. Investment in a community led renewable project needs to include a robust business case.

There is a lot of guidance available on the components of a business case. The following key components could form structure of the business case.

The project description

This should discuss the current position of the project development, the future position and potential alternatives considered. Who are the key stakeholders involved in the project and what agreements are in place between the stakeholders.

The benefit of the project

This is where the details of the potential outcomes are highlighted. This would also include the community development plan. Other information that could be provided could be details on safety, financial impact, risk management, environmental concerns and other regulatory requirements.

To determine an initial financial benefit from the project you can use the Project finance module.The minimum information that you need to use the finance model to calculate the financial viability of the project includes:

- Indicative project capacity (MW)
- Estimated capacity factor for the development

    - The developers may have a ball-park capacity factor figure they are using (for wind somewhere between 35-45% and hydro between 45-55%)
- Estimated capital costs
- Maximum size of equity investment being made available to the community eg 35-40% of total equity investment
- Minimum size of equity investment being made available to the community, eg 1% of total equity investment
- How the development of the project is likely to be structured: indicative debt/ equity gearing ratios
- Timetable for development.

If you are investing in a project being developed by a commercial developer as a minimum they should provide you with this information.

The benefit of the Project Finance module is the ability of providing investors and communities with outputs such as ***Debt Service Cover Ratios (DSCR)*** and ***net present value (NPV)*** amongst other key financial performance indicators.

These financial figures are an important part of the business case, but they are not the only considerations lenders or investors will make. The complete package of information provided in the business case will be considered.

The proposed project

This section should cover the quantitative technical details. This should detail the technology that is being proposed and its anticipated performance and costs. What is the proposed legal structure that the group is proposing to incorporate.

The CARES Investment Ready Tool is a good starting point for collating all the required technical, legal and financial information required. This should then be summarised within the business plan.

Implementation plan

This Section should outline the timetable for developing the project, including all the project tasks, who is responsible for completing them and what the key milestone dates are. If there is professional advice required, time should be allowed for procuring this support. The timetable for investing in a shared ownership project will be short. You may be required to make investment decisions in a matter of weeks, so it is important to be as prepared as possible for when the opportunity arises. The CARES Project Development Plan can be tailored for project.

Case studies

For more information on the following case studies, visit the Local Energy Scotland website.

Neilston Community Wind Farm

Location: East Renfrewshire

Project: 10MW Wind farm scheme (4 turbines)

Type of venture: Joint Venture between Carbon Free Developments Limited and the Neilston Trust

Community Stake: East Renfrewshire residents hold 28% stake, costing £950,000

Opened: May 2013

Details: This was the first joint ownership venture (JV) between a wind farm developer and a community. The Neilston Trust raised £950,000 to purchase their stake. This was partly funded by the Scottish Government and other organisation including Social Investment Scotland. It was estimated that money would start to become available for Neilston Development Trust after 2018-2019. This is common for a renewable project development where the income from energy generation will initially go to service the debt. Once the debt has been reduced and the interest payments are less, then there is excess income which is available to the owners of the project.

Allt Dearg Wind Farmers LLP

Location: Ardrishaig

Project: 10MW Wind farm scheme (12 Vestas V52 turbines)

Type of venture: Joint venture various partners

Community Stake: The Allt Dearg Wind Farmers LLP (ADWF) owns the venture but is supported by 6 partners including the Ardishaig Community Trust which has a 1/12th stake (£300,000).

Opened: 2011

Details: There are 6 owners of the Allt Dearg Wind Farm, including Ardrishaig Renewable Energies Limited (ARE Ltd) who are a company limited by shares that is wholly owned by The Ardishaig Community Trust. The investment of £300,000 by ARE Ltd was funded by a loan from ADWF. This now provides ARE Ltd with a share of the cash surplus generated by the wind farm, which is gift aided to the Ardishaig Community Trust.

The project capital was funded by the partners (20%) and a 15-year loan from the Co-operative Bank. The loan was secured against the assets and future cash flow of the partnership. The bank provided favourable terms for the project on the basis of a few

conditions and because of the end use of the revenues. These conditions related to transparency and good governance.

Two of the wind farm owners are defined as “equity investors”. Once the project has paid for the operational costs of service, maintenance, insurance and administration, the cash that remains is first used to make bank loan repayments and interest payments, and thereafter a fixed profit share payment to the two ‘equity investors’. The cash surplus that remains will then be divided between the ‘non-equity partners’, including the Trust, via ARE Ltd.

Project finance evaluation

The value of the project is determined using the model.

There are two separate stages to evaluating the financial returns on a potential investment in a renewable project. The first is to determine the financial performance of the project as a whole. The second is to evaluate the financial return of the investment offering to the community group.

One way to determine the financial performance of the project is to ask the developer for the financial model they have developed for the project. This will give full access to the assumptions that the developer has made in assessing the project. This is likely to contain some commercially sensitive information and the developer would expect you to treat it as such. However, due to this, some of the information may not be possible to obtain such as third-party information, supplier bid, annual fees paid to landowner, etc.

CARES Project finance model

The information that has been collated as part of your business plan, will allow you to use the CARES Project Finance Model to determine the financial performance of the project. Entering the information obtained when developing a business plan into the finance model will provide an indication of the financial viability of the overall project and will identify whether or not it will be possible to raise finance (the model provides further information on confirming the financial viability of a project).

The CARES Project Finance Model is not an investment model. It has been designed to provide an indication of the financial performance of small-scale renewable projects. The accuracy of the data that is entered into the model will influence the accuracy of the results that it produces.

The CARES project Finance Model will be calculating the financial viability of the overall project. The ***Internal Rate of Return*** that is calculated and the ***Total Dividends*** (total profit) calculated are for the whole project. The returns that can be anticipated by the community investor will be determined by the Investment Memorandum provided to the community group, which will outline the detail of the investment being offered to the

community. The returns for the community will also be influenced by the financing route chosen by the community group, for if different sources are secured it is quite probable that the eventual return to the shared ownership developer will be different to the community return.

Before making any investment decisions, professional advice should be sought.

Investment memorandum

Working out the potential financial return of the investment offering to the group requires careful analysis of the investment memorandum. An investment memorandum is a document that a developer presents to potential investors. It presents the investment case in the context of a detailed view of the Project Vehicle, its management team and how the project will be managed.

This will include the size of the equity investment, how long the equity invested will be held for and estimated financial returns. Professional advice from an independent financial advisor should be sought to review this and understand the level of risk involved.

The investment memorandum may give an indication of the project costs including operational costs, maintenance, insurance, and administration in addition to the finance costs. The project income will vary from year to year depending on the resource available (ie the amount of wind that blows or water than flows) and the price of electricity. Careful attention should be paid to administration costs included and different investors may be offered a different share of the profits.

There are a many different variations of the offer being made to a community. These include:

- Investment in the full development and construction phases of the project
- Investment solely in the construction phase
- Investment in the project after construction.

If a group is being offered a 10% investment stake in the project, they can expect to see a maximum 10% of the dividends. However, this is expected to cover debt repayments, etc. The Investment Memorandum will indicate the potential return that might be expected. This size of the return on the investment can be expressed in a number of different ways.

Annual return – the investment return is normally expressed as a % of the amount invested provided over a period of time. An annual return would indicate an anticipated return each year from the start of operations. It is unusual for renewable energy projects to be able to provide a fixed return each year as they have a large capital cost which needs to be paid off before any investors can expect a return.

Lifetime return – a wind project can have a lifetime of up to 25 years and a hydro plant might operate for up to 40 years and over. This should be included in the investment memorandum. It is more realistic to consider the investment return over the lifetime of the

project, with lower returns likely at the beginning of the project and higher returns later on in the project as evidenced in the case studies.

Percentage of profits – after all income and costs have been considered, the remaining profits (or dividends) will be distributed to investors. Having used the CARES Project Finance Model to give an indication of the project profits, the community investor might be offered a percentage of these profits related to the size of investment made.

Investment risks

The following list of risk factors is not exhaustive and there may be other risks which relate to an investment in a renewable development. It is essential that a group takes its own independent financial and other advice before making any decisions about the options available.

- The return derived from investment in the Project Vehicle can go down as well as up. Additionally, the entire investment made by the community vehicle could be lost.
- The value of any interest in the Project Vehicle held by the Community Vehicle could be lost.
- The financial operations of the Community Vehicle may be adversely affected by the impact of general economic conditions.
- The Community Vehicle might have no voting rights in the Project Vehicle, therefore will have no control over the direction or decisions of the Project Vehicle.
- Any investment in the Community Vehicle will be difficult to value.
- Any investment in the Community Vehicle should not be regarded as short term in nature and community groups must be prepared to take a long-term view of their investment.
- Changes in economic conditions and legislation can substantially adversely affect investments.
- The Project Vehicle may be adversely affected by external events such as fires, floods, etc.
- No representation or warranty is or can be made as to the future performance of the Community Vehicle which becomes a member of the Project Vehicle.
- The Project Vehicle may require further funding post Financial Close and if the Community Vehicle does not participate its stake may be correspondingly reduced.
- By their nature, energy generation projects have significant construction risks arising from delayed operation and commissioning, costs escalation during the construction period, environmental.