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Understanding utility contracts

Fixed versus flexible

There are two ways to agree to buy electricity and/or gas for your school or Academy; either on a "fixed" basis or in a "flexible" way. In mortgage terms, the common analogy would be to either lock in at an agreed fixed term interest rate or to float with the markets and go the 'variable' route. In essence, it depends on a schools appetite for risk.

Of the £millions schools spend each year on the procurement of electricity and gas, experts believe that an average of 5% cost reduction can be achieved by better procurement, and a further 3.5% from aggregating volumes (therefore reducing supplier margins), but this does depend on market movement.

Fixed	Flex
Contracts can be fixed for up to 4 years. Although the markets can go up or down, longer fixed term contracts have consistently outstripped flex contracts.	Only an indicative price is provided, as the energy may not yet have been purchased. This makes it difficult to budget as the markets may go up or down. The contract is reconciled at various points through the period (normally 4 years).
Invoicing is based on actual or customer reads.	Invoicing may prove difficult for suppliers due to regularly changing prices.
Different contract terms can be entered into, 12, 24, 36 or even 48 months and, if found to be unsuitable, you can change supplier/contract after 12 months.	Some Central Purchasing Bodies (CPBs) want to tie schools into 4-year agreements without any knowledge of the price. However, being locked to one supplier for 4 years may not be best practice.
Freedom of choice and information is given in a clear and transparent tender.	Choice is taken away from the SBM
Fixed contracts may mean locking into a long-term contract at the wrong time so an industry expert should be engaged.	Flex and forward contracts do provide flexibility as long as sites are not locked into for a long period. However, SBMs have no way of knowing what the purchasing policy is from the CPB.
If the decision to go to market is made at the same point each year, then it is likely that a bad decision has been made – look at what the markets are doing as you can purchase up to 12 months in advance (therefore, no different to forward contracts)	Inaccurate forecasting may mean bad decisions are made.

Many CPBs recommend flexible purchasing agreements (FPA) or purchase with purchase (PWP) to comply with European purchasing guidelines, using such organisations as LASER, GPS, ESPO, and YPO. However, many variables effect UK power markets, for example, a ten-year trend shows a 50% increase in wholesale gas prices since 2001; some as high as 100%, some down to 10%. This means that flex deals may not represent best value as they do not provide choice, security of price or budgeting, and they are dependent on clever trend analysis and understanding of market fundamentals to purchase at the right time.

Utility contracts after academy conversion

When schools convert to an Academy, novating (substituting a new contract for an old one) the energy supply agreements should be easy (in theory); same school, same usage, slightly different funding (now direct from Government), so why is it so difficult?

- Electricity and gas suppliers will see the new Academy as a new company with no trading history and no credit score and so, will apply stringent rules to the "new" account under their Change of Tenancy (CoT) rules.
- Your new Academy will invariably be faced with termination of the existing contract as your school may be "pushed" out of the Local Authority contract as it is now a company. If not, and you notify the supplier directly, they will apply the CoT and treat you as if an old tenant is moving out of the school and a new one in.

The supplier will cancel the old supply agreement (although the supply will continue, it is how much you pay for the energy which is in question here), and put the new Academy onto a default contract at potentially more than twice the cost of the earlier contract, as a new contract has not formally been put in place. As the new Academy will have no credit score, the supplier may want a security deposit (of around 3 months cost of the power) before a new contract is put in place.

Some good things may actually come from this:

- If the school's old contract is based on a high rate, and the energy markets have moved downwards, it will give you a good reason to get out of the old contract and move onto a cheaper one. Naturally, this depends very much on the current state of the energy markets and hence you should always test the market by tendering your contracts first.
- If the markets have moved against you and it is not worth entering into a new contract, try to keep the existing contract rates in place (that the supplier is trying to cancel). To do this, refrain from formally informing the supplier in writing that the school is converting to an Academy, as you will automatically slip into their CoT process. Instead, speak to your energy supplier account manager and/or Central Purchasing Body (CPB) and explain the funding agreement, letting them know that nothing within the school is changing (except bank account and perhaps name) and that a new contract does not need to be entered into, it just needs novating.