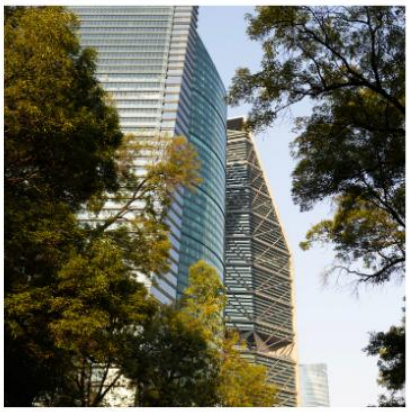
PROSPECT



Learning Handbook on Internal Contracting (Intracting)

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About the project

PROSPECT aims to strengthen the capacity of local and regional authorities (LRAs) across Europe to implement sustainable energy and climate actions by reducing reliance on public funding and increasing the use of innovative financing schemes (e.g., one-stop-shops, energy agencies, energy communities). The project offers a peer-to-peer Capacity Building Programme (CBP) tailored to the needs and time constraints of LRAs, available in multiple languages and structured in adaptable learning modules. Through large-scale outreach, including very small and remote LRAs, PROSPECT CUBE acts as an entry point to EU programmes and financing opportunities for authorities with limited experience in the field.

PROSPECT CUBE builds upon two successful Horizon 2020 initiatives: PROSPECT (2017–2020) and PROSPECT+ (2022–2025).

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List of abbreviations

Abbreviation	Description
AURA	Auvergne-Rhône-Alpes
AURA-EE	Auvergne-Rhône-Alpes Énergie Environnement
CAPEX	Capital Expenditure
CO_2	Carbon Dioxide
CoM	Covenant of Mayors
EE	Energy Efficiency
EMS	Energy Management System
ESCO	Energy Service Company
EU	European Union
GHG	Greenhouse Gas
HVAC	Heating, Ventilation and Air Conditioning
LRA	Local and Regional Authority
M&V	Monitoring and Verification
SECAP	Sustainable Energy and Climate Action Plan
SEAP	Sustainable Energy Action Plan
SLA	Service-Level Agreement
SPP	Simple Payback Period

1. Introduction

European and national governments have set ambitious objectives on the path towards climate neutrality by 2050, and local and regional authorities (LRAs) play a key enabling role in advancing this goal. As the level of governance closest to citizens, cities and regions are well placed to translate policy objectives into practical solutions that can deliver measurable energy, climate, and societal benefits at the local and regional levels, through a significant share of investments on the ground.

At the same time, however, structural budgetary constraints, including inter alia limited access to upfront capital or rigid internal financial and accounting frameworks often limit LRAs' ability to act. These constraints frequently delay or prevent the implementation of cost-effective measures, regardless of their potential to deliver long-term savings and contribute directly to broader energy and climate objectives.

In response to such challenges, innovative financing approaches have emerged to support LRAs in advancing their sustainable energy and climate actions while retaining control over assets and financial flows. One such approach is internal contracting (known also as intracting), a financing mechanism based on a revolving fund, whereby investments are financed internally and repaid through the cost savings generated by the implemented measures. Once recovered, these resources are reinvested to finance further actions, creating a self-reinforcing investment cycle.

In doing so, internal contracting enables LRAs to overcome structural financing barriers, reduce reliance on external funding sources, and strengthen internal capacities for investment planning and energy management.

1.1. Purpose of this handbook

The purpose of this handbook is to provide practical guidance to LRAs interested in designing and implementing internal contracting schemes based on revolving funds to support their sustainable energy and climate-related investments. Building on the experience gathered through previous PROSPECT initiatives and EU-wide practice, the handbook explains the concept, principles, and functioning of internal contracting, highlights its close relationship with revolving funds, and outlines the organisational, financial, and technical requirements involved in setting up and operating such schemes.

In addition, it presents key success factors, common barriers, and lessons learned from existing internal contracting experiences, with the aim of supporting informed decision-making and effective implementation. The focus is placed on replicability, practical implementation, and decision support, providing readers with actionable insights that can be adapted to different local and regional contexts.

1.2. Target audience

This handbook is primarily addressed to LRAs seeking sustainable and self-reinforcing financing solutions to support energy, climate, and sustainability-related investments, including measures identified in local and regional action plans. In particular, the target audience includes:

- Elected representatives and decision-makers responsible for setting strategic priorities, approving investment frameworks, and enabling the use of internal contracting as part of the city's or region's long-term climate and energy strategies.
- Staff from energy, environmental, technical and planning departments within LRAs, responsible for identifying and implementing concrete measures under local and regional climate action plans, and contributing to the operational design of internal contracting schemes.
- Financial departments within LRAs, undertaking a key role in managing revolving funds, ensuring budgetary alignment, and monitoring the financial flow and performance of the internal contracting arrangements.
- Local energy agencies or internal units responsible for supporting cross-departmental cooperation, providing technical expertise, and assisting in the monitoring and evaluation of implemented measures.
- Public organisations and entities involved in the delivery of energy or climate-related services, which may participate in internal contracting schemes as implementing bodies or beneficiaries.

The handbook may also be useful for other public bodies and support organisations involved in advising or supporting local and regional authorities on innovative financing approaches for climate action.

1.3. How to use this handbook

This handbook is designed as a flexible learning and reference tool, adaptable to different roles, experience levels and objectives. Readers new to internal contracting are encouraged to begin with the introductory sections to understand the mechanism and its potential benefits, while more experienced practitioners may focus on organisational setup, financial management and operational procedures.

The handbook follows a step-by-step structure, guiding readers from the basic principles of internal contracting to practical implementation and real-world examples. While each section can be read independently, together they provide a coherent overview of how revolving fund-based internal contracting schemes can be developed and operated by LRAs.

2. Understanding the internal contracting

Internal contracting (also referred to as intracting) is a financing and organisational model that enables LRAs to plan, finance and implement energy efficiency (EE) and other climate-related investments using their own internal resources and repayment mechanisms. Rooted in the logic of revolving funds, internal contracting links upfront investment to verified cost savings, allowing recovered resources to be reinvested over time on a continuous and self-reinforcing basis (Schäfer & Schilken, 2017). In this way, internal contracting supports a shift from one-off, project-based financing towards a more strategic and long-term investment approach (Todeschi et al., 2025).

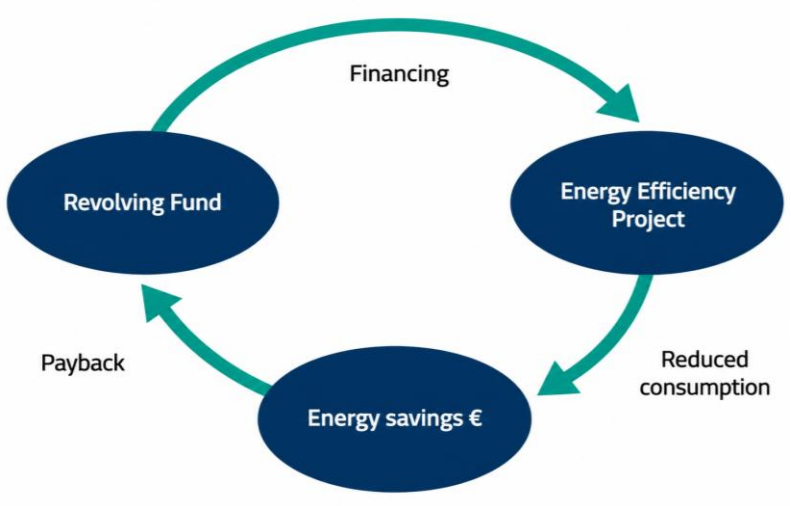

Figure 1. Typical functionality of internal contracting including a revolving fund

(Source: Schäfer & Schilken, 2017)

Focus Box 1: How internal contracting is formalised?

Unlike external contracting or third-party financing models, internal contracting keeps financial flows, responsibilities and decision-making processes within the public authority. This internalisation provides greater control over investments, reduces exposure to external financing costs, and supports long-term capacity-building related to energy management, financial planning and project implementation.

Usually, no external contractual relationships are involved. Instead, arrangements are formalised through internal decisions, administrative procedures or service-level agreements (SLAs). These instruments:

- Help clarify roles, repayment rules and monitoring responsibilities, supporting transparency and accountability across departments,
- facilitate coordination and long-term cooperation within the LRA, and
- enable the implementation of smaller-scale or less financially attractive measures often overlooked under external contracting models.

2.1. How it works in practice?

In practice, internal contracting follows a closed investment and repayment cycle that links upfront financing to performance-based savings. The process starts with the identification and assessment of suitable measures, based on technical analyses, energy audits, or priorities defined in local or regional energy and climate plans, considering also expected costs, savings potential, and payback periods. Once approved, the measures are financed upfront often through an internal revolving fund and implemented by the relevant internal departments or, where appropriate, by external contractors procured by the authority (Todeschi et al., 2025).

Following project implementation, the resulting cost savings - typically from reduced energy consumption or operating costs - are used to repay the initial investment to the fund over an agreed period, in line with a predefined internal arrangement (Schäfer & Schilken, 2017).

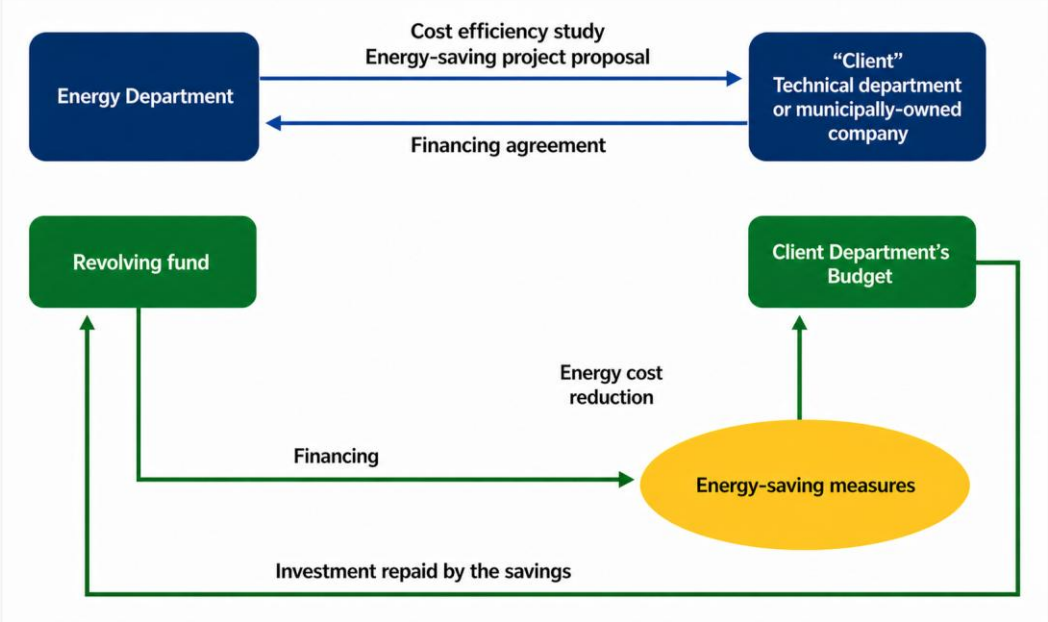

Figure 2. Internal contracting financing scheme including a revolving fund
(Source: Schäfer & Schilken, 2017)

The recovered capital is then reused for subsequent actions, enabling a continuous investment cycle. This repayment logic allows LRAs to scale up investments over time, while reducing reliance on annual budget allocations (Junghans & Dorsch, 2015; Novikova et al., 2017).

2.2. Arrangements, types and characteristics

Internal contracting schemes can be designed in different ways, depending on the administrative structure, financial rules, and strategic priorities of LRAs. While the core principle - financing investments internally and repaying them through savings - remains constant, internal contracting differs in how it is organised, financed, and managed.

Across different contexts, internal contracting follows a shared internal financing logic, while allowing flexibility in governance, operational design and financial flows.

2.2.1. Arrangements

Internal contracting relies on clear governance and financing arrangements that define responsibilities, decision-making processes, and financial flows within an LRA. Moving beyond the technical details of individual project implementation, these arrangements provide a stable structure that allows the scheme to operate effectively over time, independently of individual projects or annual budget cycles (Novikova et al., 2017; Schäfer & Schilken, 2017; Todeschi et al., 2025).

In terms of initial capital, in most cases financing is provided from the municipal budget, either through direct internal allocations or through a dedicated revolving fund or trust. Although not mandatory, where a revolving fund is used, internal contracting can be understood as a practical variation of the model, enabling EE and other emission-reduction measures to be financed through the reinvestment of the savings generated by earlier measures, usually at a 0% interest rate and without additional charges (Irrek et al., 2005; Limaye et al., 2014). External sources, such as grants, may also be mobilised to complement these resources and strengthen long-term sustainability of the scheme (C40 Cities, 2016; ESMAP, 2014).

In operational terms, a specific internal unit - often located within an energy, environmental, financial, or cross-cutting coordination department, or within a municipally owned entity with relevant expertise -is appointed to coordinate or manage the scheme's function. Acting in an ESCO-like manner, this unit assesses savings potential, plans investments, oversees resource allocation, and monitors repayments, while other departments remain responsible for implementing measures within their respective areas of expertise, drawing on existing internal know-how (Junghans & Dorsch, 2015; Todeschi et al., 2025).

2.2.2. Types of internal contacting based on a revolving fund

Although internal contracting is most commonly associated with - and almost exclusively implemented through - internal revolving funds, its financing structure may also depend on the nature of the revolving fund itself, which can be either internal or external. In practice:

- external revolving funds re typically managed by third-party organisations - such as utilities, fund managers or dedicated entities - that provide financing to multiple LRAs under agreed repayment conditions; in some cases, external service providers, such as ESCOs, may also be contracted to implement measures on behalf of participating authorities (ESMAP, 2014; Limaye et al., 2014).
- internal revolving funds, are established, capitalised and managed by a single LRA, remaining closely aligned with internal decision-making and budgetary frameworks; under this arrangement, the authority provides the initial capital for its own investments, allocates resources and recovers costs through the generated savings (ESMAP, 2014; Schilken & Wyssling, 2013).

Beyond the financing structure, the organisational configuration of the scheme can also vary significantly, with LRAs typically adopting one of the following approaches:

- Centralised approach, where a single coordinating unit within the authority manages the fund and oversees investments across departments[1].
- Decentralised approach, where individual departments or units propose and implement measures within a shared internal financing framework[2].

To identify the most appropriate governance setup, LRAs can assess their institutional capacities, operational practices and strategic objectives against a set of key criteria, as outlined in Table 1.

Table 1. Comparison of centralised and decentralised internal contracting models

Criteria	Centralised model	Decentralised model
Organisational fit	Appropriate for centralised structures with strong coordination in place	Suitable for structures with operational autonomy across departments and established internal capacities.
Governance structure	A single coordinating unit manages the revolving fund and oversees investments across the authority.	Multiple departments or units propose and implement measures within a shared internal financing framework.
Technical capacity	Requires a strong, specialised internal unit with expertise across sectors.	Relies on distributed technical knowledge embedded within individual departments or units.

[1] This is best exemplified by the Stuttgart practice, which focuses on technical efficiency and rapid fund recapitalisation (NetZero Cities, 2025)
[2] The Udine practice follows this path, using shared savings as an incentive for departmental participation (Energy Cities, 2017)

Administrative control	High level of control, with standardised procedures, reporting, and monitoring through one central entity.	Moderate control, requiring clear coordination mechanisms and internal agreements.
Financial incentives	All savings are channelled back to the revolving fund, maximising reinvestment speed and financial consolidation.	Savings are shared, with a portion retained by departments to encourage ownership and engagement.
Project focus	Well-suited to large-scale, cross-cutting, or systemic investments.	Particularly effective for smaller, diverse, or incremental actions.
Relationship with revolving funds	Linked to a single internal revolving fund managed centrally; external funds rarely used.	Linked to a shared internal revolving fund, sometimes combined with external funding sources.

Finally, internal contracting schemes may also differ in scope and strategic positioning. They can operate either as standalone financing tools dedicated to specific measures or as part of broader climate, energy or sustainability funds supporting a wider portfolio of actions. In the latter case, they function as a core financing mechanism within an integrated investment framework, helping align individual projects with long-term policy objectives (EURAC Research, 2017; Schäfer & Schilken, 2017; Schilken & Wyssling, 2013).

Focus Box 2: What makes internal contracting different?

Taken together, these characteristics explain how internal contracting performs in practice, supporting a strategic and long-term approach to investment for LRAs.

- Administratively and legally, it relies on simplified internal procedures and agreements, enabling faster decision-making and reducing contractual complexity.
- Financially, it avoids external interest rates and profit margins, allowing savings to remain within the authority and be reinvested over time.
- Technically, it retains know-how internally, strengthening institutional learning and capacity.

This integrated approach enables LRAs to maintain a high level of control and flexibility over investments, reduce reliance on external actors, and deliver strategic energy and climate actions in a more coherent and sustained way.

2.2.3. Key characteristics: Internal vs external contracting

Internal contracting is characterised by a combination of administrative, financial, legal, and technical features that distinguish it from external contracting or third-party financing models. Fundamentally, the key difference lies in the internal allocation of financing, decision-making and implementation responsibilities within the public authority (Schilken & Wyssling, 2013).

While external contracting relies on third-party investors or service providers, internal contracting keeps these elements within the authority itself, a distinction that has important implications for the implementation speed, risk allocation, financial performance, and institutional learning.

A comparative overview of the main distinguishing characteristics of internal and external contracting approaches is given in Table 2 below.

Table 2. Comparison of internal and external contracting models

Dimension	Internal contracting	External contracting
Administrative efficiency	High: Managed within the authority; Streamlined procedures; Fast decision-making	Low: Requires external procurement, audits, and often lengthy contract negotiations
Governance & control	High: Full internal control over priorities, investments, and implementation	Low: Control is shared with or transferred to third parties (e.g. ESCOs, financial institutions)
Legal (contractual) complexity	Low: Based on internal decisions, procedures, or service-level agreements	High: Based on complex external contracts with legally binding guarantees
Financial	Low: Financed through internal resources, with no interest rates or profit margins; Savings remain within LRAs	High: Financed through external capital; Includes interest, profit margins, and transaction costs
Risk allocation	Internal: Risks assumed and managed internally by the LRA	Transferred: Risks moved to external providers, often at a cost or premium
Investment scope	High (broad): Enables small-scale, systemic or less profitable measures	Low (Selective): Focuses mainly on highly profitable measures with short payback periods
Technical expertise	High (internal): Know-how remains within LRAs, supporting long-term capacity	Low (Outsourced): Relies on external expertise; limits internal skill development
Monitoring & verification (M&V) complexity	Low: Based on internal monitoring systems and simplified procedures	High: Requires formal M&V, and strictly contractual performance guarantees
Flexibility	High: Easy to adjust project scope or priorities as municipal needs evolve	Low: Any adjustments require complex and costly contract renegotiations
Public Value	High: Maximises benefit by reinvesting saving in new actions.	Low: Benefit is shared with private entities to cover risks and profits.

2.3. Why internal contracting matter? Benefits and added value for LRAs

For LRAs internal contracting is more than a financial tool; it is a strategic governance model that empowers them to take full control of their energy transition, providing a structured pathway to overcome the budgetary and procedural constraints that frequently stymie local climate action (Andreanidou et al., 2018; Schäfer & Schilken, 2017; Schilken & Wyssling, 2013; Todeschi et al., 2025). Primarily, the political rationale for its adoption rests on the following three pillars:

SECURING LONG-TERM FINANCIAL RESILIENCE AND PUBLIC VALUE. Internal contracting provides a stable and self-reinforcing framework that strengthens long-term sustainability of local investments by:

- creating a self-sustaining investment cycle through its revolving logic,
- ensuring predictable and scalable financing, independent of annual budget cycles and reducing reliance on commercial interest rates and third-party profit margins,
- maximising public value, as all savings are retained within the authority and reinvested into local infrastructure and services, amplifying long-term community benefits.

EMPOWERING INSTITUTIONAL LEADERSHIP AND STRATEGIC COHERENCE. Beyond financial benefits, internal contracting strengthens institutional capacity and governance by:

- retaining technical and financial expertise internally, fostering an institutional learning effect and supporting more informed and autonomous decision-making,
- demonstrating ownership and leadership, reinforcing accountability, transparency and long-term policy continuity,
- enhancing cross-departmental coordination, linking technical performance with financial recovery and supporting a coherent approach to sustainability.

CATALYSING COLLABORATION, COMMITMENT AND MOMENTUM. Internal contracting's true added value lies in its ability to drive positive cultural and institutional change. By creating an accessible financing mechanism for smaller, bottom-up efficiency projects, it empowers the LRA from within, leading to:

- broader participation, fostering collaboration across departments, breaking down silos and building a shared sense of purpose.
- stronger engagement and ownership, generating collective momentum through the visible success of multiple small initiatives.
- embedding climate action into daily operations, transforming it into a sustained organisational practice.

2.4. Sector-wide application: When and where internal contracting can be used?

Internal contracting can be applied across a wide range of sectors and organisational contexts, provided that measures generate measurable cost savings that can be monitored and reinvested through the internal financing mechanism (Andreanidou et al., 2018; Schäfer & Schilken, 2017; Schilken & Wyssling, 2013). Its flexibility makes the scheme suitable both for comprehensive investment programmes and for incremental improvements implemented over time, where it can be used to:

- support long-term renovation or optimisation programmes,
- finance pilot actions and smaller-scale measures, and
- complement other funding sources as part of broader investment frameworks.

At the same time, its internal nature allows diverse actions to be bundled across different departments or service areas, supporting a more integrated investment strategy.

Overall, wide adaptability of internal contracting makes it a versatile tool that can evolve alongside LRAs' priorities, capacities, and policy objectives.

In practice, the model is particularly attractive for projects related to energy-savings measures in public assets under the direct operational control of LRAs, where savings can be clearly attributed and recovered. Beyond these, it is also well-suited for cross-cutting measures that improve operational efficiency, reduce resource consumption, or enhance system performance (Novikova et al., 2017).

Typical internal contracting applications are presented in Table 3.

Table 3. Scope and strategic function of internal contracting applications

Category	Typical applications	Strategic function within the scheme
Energy systems	Optimisation of heating, cooling (HVAC), ventilation, and lighting (e.g. LED upgrades)	Core function: Generates stable and measurable savings that help replenish the internal fund
Building envelope	Roof and wall insulation, window replacement, weatherisation measures	Synergistic function: Supports deeper renovations when combined with faster-payback measures
Operational efficiency	Energy management systems (EMS), smart sensors, automated controls	Enabling function: Improves monitoring, savings verification and financial management
Cross-cutting measures	Water efficiency, fleet management, resource optimisation in municipal services	Diversification function: Expands the revolving approach to broader sustainability actions

Programmatic approach (long-term)	Multi-year investment pathways supporting the systematic upgrade or optimisation of assets and services.	Stability function: Supports long-term investment planning across budget and political cycles.
Incremental approach (short-term)	Small-scale actions including innovative technologies or targeted departmental improvements.	Agility function: Enables smaller or innovative actions often overlooked by external financing models.

To ensure effective implementation across sectors, internal contracting schemes are often supported by clear, integrated frameworks covering project eligibility, prioritisation, and repayment. Drawing on practical experience from LRAs – as for example the Udine case - such frameworks can help guide the selection of measures that balance environmental impact with financial viability, while safeguarding the revolving nature of the financing mechanism through transparent monitoring and repayment rules.

Table 4. Example of a project selection, prioritisation, and repayment framework in internal contracting schemes

Framework component	Criteria/Aspects	Description / Typical application
Project eligibility	Asset ownership	The intervention applies to assets owned and operated by the authority
	Verified baseline	A clear pre-intervention energy or cost baseline is established to enable reliable savings verification.
	Technical feasibility	The project is supported by a technical feasibility assessment validated by an internal unit.
Project prioritisation	Energy savings	Expected reduction in energy consumption often subject to a minimum threshold (e.g. ≥10%).
	Financial viability	Simple Payback Period (SPP) within an agreed timeframe (commonly <10–12 years) to preserve the revolving nature of the financing mechanism.
	CO_2 impact	Estimated annual reduction in greenhouse gas (GHG) emissions, supporting climate targets.
	Strategic alignment	Contribution to local energy and climate strategies (e.g. SEAPs/SECAPs).
	Innovative or replicable potential	Use of innovative or scalable solutions applicable across departments or services.
Repayment & monitoring	Repayment duration	Repayment period aligned with the expected payback time, often including a buffer (e.g. 1–2 years) to ensure full recapitalisation of the fund.
	Savings verification	Regular verification of achieved savings by a designated internal or municipal body.
	Incentives	In some cases, departments may retain part of surplus savings as a performance incentive.
	Maintenance responsibilities	Operation and maintenance remain with internal departments , while capital expenditure (CAPEX) is covered by the fund.

2.5. Main stakeholders involved

The effective design and operation of an internal contracting scheme rely on the active involvement and coordination of several internal stakeholders within an LRA. While the exact arrangements may vary depending on institutional structures and local context, a clear allocation of roles and responsibilities is essential to ensure transparency, accountability, and the long-term success of the scheme.

Table 5. Main stakeholders typically involved in internal contracting schemes

Actors	Typical role in intracting	Key responsibilities
Political leadership	Strategic oversight and endorsement	Approves the establishment of the scheme; Provides political commitment; ensures alignment with energy, climate, and sustainability objectives; Supports allocation of initial capital.
Financial/budget department	Financial governance and control	Sets up and oversees the financial architecture; Manages budget allocations and accounting arrangements; ensures compliance with financial rules; Monitors repayments and fund replenishment.
Coordinating/ managing unit	Day-to-day scheme management	Coordinates internal contracting activities; assesses savings potential; Allocates resources; Monitors performance and repayments; Acts in an internal ESCO-like role across departments.
Technical departments/ services	Project development and implementation	Identify and propose measures; Provide technical input; Implement projects within their areas of competence; ensure operational feasibility and quality of implementation.
Implementing departments/asset managers	Operational delivery and ownership	Deliver measures on the ground; Manage assets affected by interventions; Contribute to monitoring data; Ensure proper operation and maintenance of installed solutions.
Monitoring and verification (M&V) function	Performance tracking and verification	Verifies achieved savings; supports transparent reporting; Ensures credibility of results; Provides evidence for financial recovery and reinvestment decisions.

3. Setting up an internal contracting: A quick step-by-step guide

Setting up an internal contracting scheme based on a revolving fund may initially appear administratively and financially complex. In practice, however, the process becomes significantly more manageable when approached through a structured and phased methodology, where each step progressively builds the institutional, financial and operational foundations of the scheme.

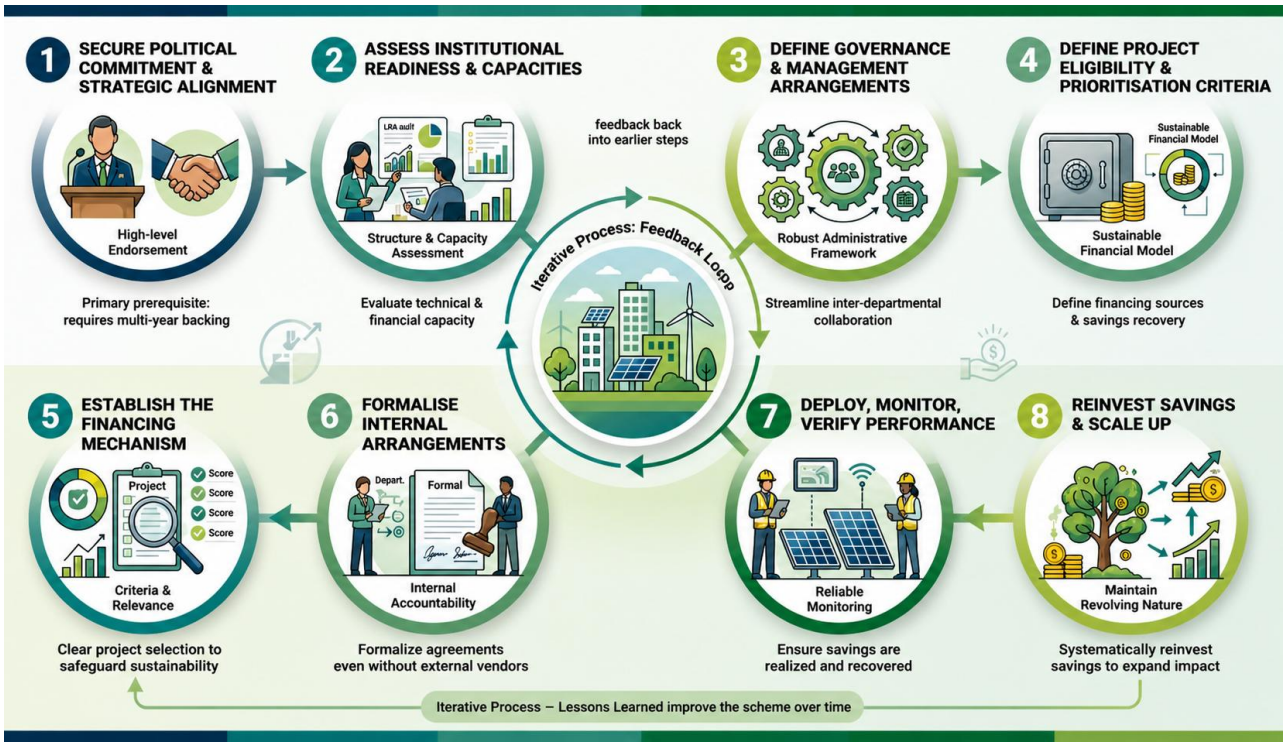

Figure 3. Key steps in setting up an internal contracting scheme with a revolving fund

While local contexts may differ, this section presents a practical step-by-step roadmap covering the main stages involved in designing and launching an internal contracting mechanism - from securing political commitment and assessing institutional readiness to establishing governance structures and financing arrangements. It then concludes with a checklist summarising the key considerations and enabling conditions that can support the successful development and long-term operation of the scheme.

Rather than prescribing a rigid model, the proposed approach is intended as flexible guidance that can be adapted to different administrative, legal and financial contexts.

3.1. From planning to operation: Key implementation steps

The following steps present the core actions and decisions typically involved in establishing and operating an internal contracting scheme, together with common challenges encountered by LRAs during implementation. In general, the process is inherently iterative, allowing lessons learned to feed back into earlier stages and progressively strengthen the scheme over time.

Step 1 – Secure political commitment and strategic alignment

Strong political commitment is the foundation of any internal contracting scheme, helping ensure continuity across budget cycles and administrative terms. Achieving this typically involves actions such as:

- securing formal political approval to establish the scheme,
- defining clear strategic objectives aligned with broader local energy and climate strategies.

Early high-level endorsement helps secure long-term support, align the initiative with strategic priorities, and create the necessary institutional conditions for sustained implementation and cross-departmental cooperation.

Common pitfalls to avoid:

- treating the scheme as a purely technical exercise rather than a strategic policy tool,
- failing to establish sufficient institutional ownership and long-term administrative commitment.

Step 2 - Assess institutional readiness and internal capacities

Before launching the scheme, LRAs should assess whether the necessary capacities are in place. Identifying gaps early allows adapting the scheme design, simplify procedures or plan targeted capacity-building measures.

Key areas to consider typically include:

- financial and accounting rules governing internal budget transfers and reinvestment cycles,
- availability of technical expertise in areas such as energy auditing and project management,
- data quality and availability for establishing baselines and monitoring savings,
- previous experience with internal financing instruments or similar mechanisms.

This step helps ensure that the internal contracting model is built on realistic foundations and adapted to the authority's organisational context.

Step 3 - Define governance and management arrangements

Clear governance structures are essential to ensure accountability, coordination and efficient implementation. Achieving this typically involves actions such as:

- appointing a dedicated steering or management unit to act as the primary anchor for the scheme,
- explicitly mapping out the responsibilities of financial, technical, and executive departments to clearly assign roles and eliminate overlaps,
- defining standardised internal decision-making procedures for swift project evaluation, approval, and continuous monitoring.

Internal contracting schemes operate most effectively when clearly assigned roles and responsibilities as well as streamlined decision-making pathways are defined from the outset.

Common pitfalls to avoid:

- weak coordination structures and unclear accountability,
- overly complex, bureaucratic workflows that may slow or delay implementation.

Step 4 - Establish the financing mechanism

This step focuses on defining how investments will be financed and how savings will be recovered to maintain the revolving logic of the scheme. Key actions may include:

- setting up a simple and operational revolving financing structure, with clear fund allocation and recovery rules,
- identifying complementary funding sources beyond municipal budget,
- defining repayment rules linked to verified savings, while ensuring compatibility with the existing accounting procedures.

Modest and easy-to-manage financing structures often prove more effective than overly complex setups, while also helping LRAs build confidence and operational experience before scaling up.

Common pitfalls to avoid:

- insufficient initial capitalisation of the fund,
- overcomplicating the financial structure and setting unrealistic repayment periods that weaken the revolving mechanism.

Step 5 - Define project eligibility and prioritisation criteria

This step establishes the criteria used to select and prioritise projects, ensuring that investments remain both financially viable and strategically aligned with local objectives. Key actions typically include:

- defining minimum eligibility requirements and establishing prioritisation criteria such as expected energy and CO_2 savings, payback period and contribution to broader local or regional strategies,
- balancing quick-payback interventions with longer-term or systemic measures.

Using a simple scoring matrix or decision-support tools such as the SYNERGISE+, developed under the PROSPECT initiative, helps ensure transparency and internal buy-in during project prioritisation.

Common pitfalls to avoid:

- insufficient transparency in project evaluation and approval processes,
- relying on vague or overly broad selection criteria, and prioritising only short-payback projects at the expense of long-term impact.

Step 6 - Formalise internal arrangements

Even without external contractors, internal accountability and operational procedures should be formally defined to ensure continuity, clarity and long-term reliability. This is typically achieved through:

- formal administrative acts or municipal decisions,
- service-level agreements (SLAs) between departments,
- internal procedures defining repayment, monitoring and reporting obligations.

A clearly structured framework helps ensure consistency across departments and enables the scheme to operate effectively despite administrative or organisational changes over time.

Common pitfalls to avoid:

- relying on informal arrangements without clear documentation,
- unclear monitoring or repayment responsibilities,
- weak internal compliance or enforcement procedures.

Step 7. Deploy, monitor and verify performance

Once projects are approved, effective implementation and reliable monitoring become essential to ensure that expected savings are achieved and recovered. Key actions in this step may include:

- providing technical support to the participating departments during the project implementation,
- verifying energy and cost savings against agreed baselines through appropriate M&V procedures,
- establishing corrective mechanisms to address underperformance or deviations where necessary.

Long-term success depends on the ability to continuously track results, identify issues early and maintain confidence in the scheme's performance over time.

Common pitfalls to avoid:

- treating M&V as a one-time reporting exercise rather than a continuous management process,
- allowing underperformance to persist without timely corrective action,
- weak coordination between implementing units, limiting the reliability of reported savings.

Step 8. Reinvest savings and scale up

Reinvesting recovered savings is essential to preserving the revolving nature of the scheme and progressively expanding its impact. Over time, this allows internal contracting to evolve from a project-based mechanism into a stable long-term financing approach.

Key actions in this step typically include:

- replenishing the revolving mechanism through recovered savings to support future investments,
- gradually expanding the scope of the scheme as internal capacity and experience grow,
- adjusting procedures based on implementation experience and performance results,
- introducing safeguards to address external factors such as energy price volatility.

Reserve buffers and periodic review mechanisms can help strengthen financial resilience and maintain the long-term stability of the scheme under changing external conditions.

Common pitfalls to avoid:

- redirecting recovered savings to unrelated budgetary needs,
- expanding the scheme without sufficient financial stability measures or operational capacity.

3.2. Internal contracting checklist – Key questions for successful set up

Following the presentation of the key setup steps, the checklist below supports LRAs in streamlining the launch of internal contracting schemes, from readiness assessment to implementation oversight.

Step 1 – Political commitment & alignment

☐ Has formal political approval been secured and aligned with broader energy and climate strategies?

☐ Are the objectives of internal contracting clearly defined?

Step 2 – Institutional readiness

☐ Are financial, accounting and organisational structures compatible with the scheme?

☐ Are sufficient technical expertise and reliable baseline data available?

Step 3 – Governance & management

☐ Has a coordinating unit been designated?

☐ Are roles and responsibilities clearly assigned across departments?

☐ Are decision-making procedures clearly defined?

Step 4 – Financing mechanism

☐ Is a functioning internal financing mechanism (e.g. revolving fund) in place?

☐ Are sources of initial capital (budget, grants) identified?

☐ Are repayment rules simple and realistic?

Step 5 – Project eligibility & prioritisation

☐ Are eligibility requirements (ownership, baseline, feasibility) and prioritisation criteria clearly defined and aligned with strategic objectives?

☐ Is there a balance between short-term and long-term investments?

Step 6 – Formalisation

☐ Are internal arrangements (e.g. SLAs, decisions, procedures) formally documented?

☐ Are responsibilities for repayment, monitoring and reporting clearly defined?

☐ Is continuity ensured beyond individual projects?

Step 7 – Implementation & monitoring

☐ Are responsibilities for implementation clearly defined and assigned?

☐ Are savings monitored and verified regularly?

Step 8 – Reinvestment & scaling-up

☐ Are recovered savings systematically reinvested?

☐ Is performance regularly reviewed and the scheme adapted or expanded over time?

4. Case study: Energy savings funds in the Auvergne-Rhône-Alpes region (France)

The “Energy Saving Funds” initiative was developed by Auvergne-Rhône-Alpes Énergie Environnement (AURA-EE) to help LRAs in the Auvergne-Rhône-Alpes (AURA) region overcome two primary barriers to energy renovation: constrained borrowing capacity and limited technical expertise. It is based on an internal contracting scheme (“intracting” funds), designed to enable the reinvestment of energy savings into new efficiency measures.

General context. In the AURA region, energy costs can represent over 20% of a municipality’s general expenses, creating an urgent need for sobriety measures to protect operational budgets. Rather than relying on external debt, the AURA-EE model creates a self-sustaining internal fund where energy-saving investments are funded by the very savings they generate.

How intracting was applied. The AURA-EE model has been implemented across municipalities in the AURA region, with the city of Albertville serving as a reference example.

The implementation begins with an “ignition” phase, where past energy savings are redirected into a dedicated investment budget used to finance “ready-to-implement” measures - such as lighting upgrades or building improvements - that generate rapid savings and support subsequent investments. This "virtuous circle" provides a practical pathway for municipalities to overcome investment barriers, and strengthen their financial autonomy.

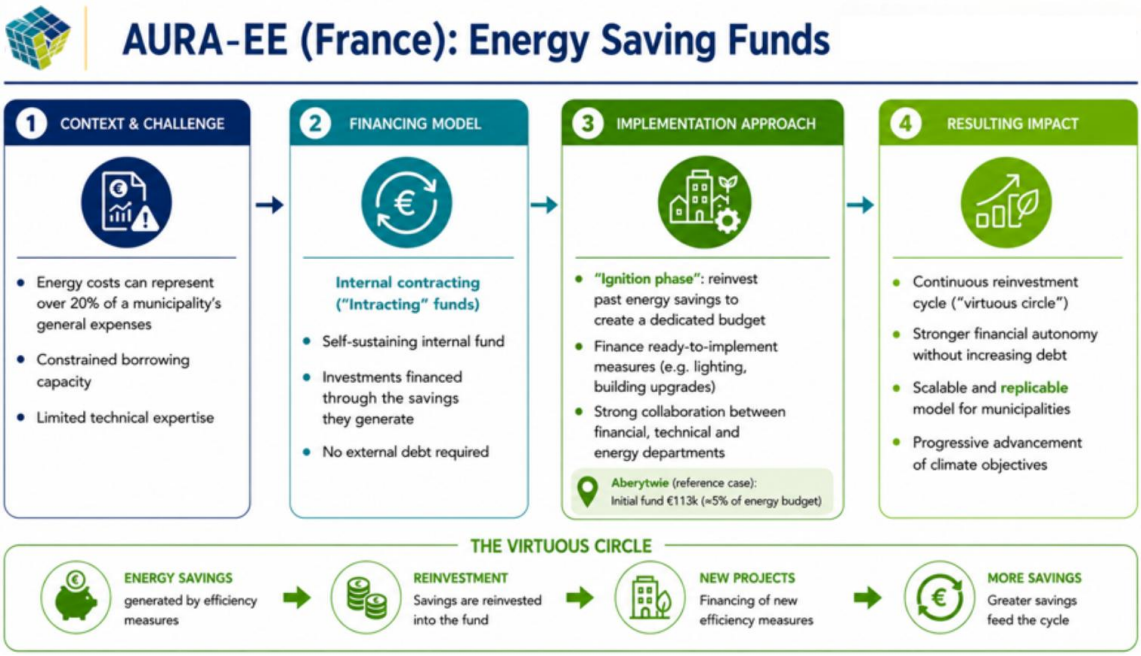

Figure 4. The AURA-EE intracting model

To facilitate replication, AURA-EE developed a capacity-building programme combining training sessions on strategy, finance and technical implementation with a dedicated "Intracting Toolbox", created in partnership with ACTEE. The toolbox (available in French) provides municipalities with practical resources, including standardised templates and implementation guides for both equity-based and loan-based models.

KEY TAKEAWAY. The strength of the AURA-EE model lies in its simple yet robust financial logic, combined with structured collaboration between financial, technical and energy departments. Supported by practical tools and clear guidance, the approach enables even small investments to generate a strong multiplier effect, delivering sustained financial autonomy alongside long-term environmental benefits.

READ MORE ABOUT THIS PRACTICE. For deeper insights on the Energy Saving Funds initiative in the AURA region, find and download the case study factsheet on the PROSPECT Stories webpage.

For further information on the agency's role broader role in sustainable energy management visit the official AURA-EE website.

Through the PROSPECT initiative, LRAs are supported in strengthening their capacity to develop and scale innovative financing schemes, drawing on an EU-wide repository of success Stories.

5. Critical conditions influencing an internal contracting

The effectiveness and long-term viability of internal contracting schemes are shaped by a set of interrelated institutional, financial, and operational conditions. While the scheme offers a robust framework for financing energy and climate actions through internal repayment mechanisms, its performance depends on how these conditions are addressed during design, implementation, and day-to-day operation. This section highlights the key factors that enable or constrain success, assesses key risk dimensions, and distils the critical elements that determine whether internal contracting can deliver sustained results in practice.

5.1. Drivers and success factors

Key drivers and enabling conditions that support successful internal contracting schemes include:

- Strong political and senior management commitment, ensuring long-term support for internal financing arrangements and repayment mechanisms.
- Clear strategic alignment with local energy and climate objectives, strengthening internal legitimacy and prioritisation.
- Well-defined governance and management arrangements, including a designated internal coordinating unit responsible for oversight, monitoring, and financial recovery.
- Availability of internal financing resources, typically through budget allocations or an internal revolving logic, enabling upfront investment.
- Realistic savings assumptions, based on robust baselines and technical assessments.
- Transparent internal rules governing project selection, repayment, and monitoring.
- Retention of expertise and institutional learning, as financial and technical know-how remains within the organisation.

5.2. Barriers and limitations

Internal contracting schemes may face a number of barriers and structural limitations, including:

- Rigid internal budgetary or accounting frameworks, complicating internal transfers and repayment arrangements.
- Limited availability of upfront internal capital, constraining the scale or pace of implementation.
- Insufficient technical or financial capacity, particularly for project preparation, monitoring, and verification.

- Resistance from implementing departments, especially where repayment obligations are perceived as restrictive.
- Complex or unclear internal procedures, undermining efficiency and slowing decision-making.
- Limited institutional experience with internal financing and performance-based repayment models.

5.3. Key risk dimensions

Several risk dimensions should be actively managed to safeguard the performance of internal contracting schemes:

- Financial risk, arising when actual savings fall short of projections, affecting repayment flows.
- Baseline risk, linked to poor-quality energy or cost data undermining savings verification.
- Governance risk, resulting from unclear roles, weak coordination, or insufficient oversight.
- Operational risk, including delays in implementation or inadequate monitoring.
- Continuity risk, where recovered savings are not systematically reinvested into new actions.
- Political risk, associated with changing priorities or leadership over time.

Focus Box 3: What makes internal contracting work?

Internal contracting schemes are most effective when a set of critical conditions are addressed in a coherent and sustained manner. These may include:

- Sustained political commitment, anchoring the scheme beyond individual projects or budget cycles.
- Clear internal governance structures, ensuring accountability and effective cross-departmental coordination.
- Sound financial design, based on realistic savings assumptions and transparent repayment workflows.
- Robust M&V systems, maintaining confidence in performance and financial recovery.
- Disciplined reinvestment practices, preserving the internal revolving logic over time.
- Adaptive management approaches enabling continuous improvement through operational experience and learning.

When these conditions are in place, internal contracting can function as a durable, flexible, and scalable financing model, enabling LRAs to deliver sustained energy and climate action while retaining control over investments and internal expertise.

5.4. Synthesis of critical conditions affecting internal contracting implementation

Table 6 below synthesises the key drivers, barriers, and risk dimensions influencing internal contracting schemes and highlights practical mitigation measures that can be applied to strengthen implementation. It provides a consolidated overview to support both strategic decision-making and day-to-day scheme management.

Table 6. Summary of critical conditions influencing internal contracting schemes

Dimension	Key drivers or enabling factors	Common barriers or risks	Mitigation measures and practices
Political & institutional	• Political commitment • Senior management support • Alignment with broader local/regional energy and climate strategies	• Shifting political priorities • Lack of ownership across departments	• Formal political endorsement • Clear mandate for the coordinating unit • Regular reporting to decision-makers
Governance & organisation	• Clear roles and responsibilities • Designated coordinating (internal ESCO-like) unit	• Unclear accountability • Fragmented decision-making	• Defined governance structure • Internal agreements or SLAs • Simple, transparent procedures
Financial design	• Availability of internal capital • Realistic savings assumptions • Clear repayment rules	• Insufficient upfront capital • Overestimated savings • Weak repayment discipline	• Start with modest scope • Conservative savings estimates • Clear repayment schedules
Technical & data	• Reliable baselines • Internal technical expertise	• Poor data quality • Limited monitoring capacity	• Standardised audits and baselines • Gradual capacity-building • Use of monitoring tools
Operational	• Simple project selection criteria • Efficient internal procedures	• Implementation delays • Administrative complexity/Bureaucracy	• Phased implementation • Streamlined approval processes
Continuity & scaling	• Disciplined reinvestment of savings • Learning-by-doing approach	• Savings not reinvested • Scheme treated as one-off	• Protect internal financing mechanism • Periodic reviews and adjustments

6. Summary of key takeaways

WHAT IS INTERNAL CONTRACTING ABOUT? Internal contracting (or intracting) is an internal financing and implementation model that enables LRAs to plan, finance, and deliver energy and climate actions using their own resources. Through this model investments are financed upfront internally and repaid over time through verified cost savings, creating a self-sustaining mechanism that supports continuous reinvestment.

By keeping financial flows, decision-making, and technical expertise within the organisation, internal contracting strengthens institutional capacity while reducing reliance on external financing and complex procurement procedures.

HOW IS INTERNAL CONTRACTING STRUCTURED IN PRACTICE? In practice, internal contracting is typically organised around an internal revolving mechanism or equivalent budgetary arrangement. A dedicated coordinating unit, often operating in an internal ESCO-like role, manages project selection, implementation support and financial recovery.

Projects are financed upfront using internal capital, and participating departments repay the investment over time based on verified savings. Clear governance structures, monitoring procedures and repayment rules are essential to ensure transparency, accountability and continuity.

WHAT ARE THE MAIN INTERNAL CONTRACTING APPROACHES AND APPLICATIONS ACROSS SECTORS? Internal contracting is typically based on internal revolving funds, where recovered savings are reinvested into new projects, creating a continuous financing cycle. These funds are established, capitalised and managed by the LRA itself, ensuring full alignment with internal decision-making and budgetary frameworks.

While similar mechanisms may be managed externally by third-party organisations, internal contracting specifically refers to models managed within the LRA.

From an organisational perspective, the scheme is typically structured in two ways:

- Centralised model, where a dedicated coordinating unit manages the fund and oversees investments across departments,
- Decentralised model, where individual departments propose and implement projects within a shared financing framework.

The model is highly adaptable and can be applied across multiple sectors, including EE in public buildings, upgrades to heating, cooling and lighting systems, as well as cross-cutting operational improvements.

Bundling projects across departments allows LRAs to balance short-term returns with longer-term strategic investments.

WHO SHOULD USE INTERNAL CONTRACTING? Internal contracting is particularly suited for LRAs that:

- own and/or manage over buildings, infrastructure, or services where savings can be measured,
- seek to retain control over investment decisions and financial flows,
- aim to strengthen internal capacities in energy management and financial planning,
- want to complement external funding sources with a robust internal financing mechanism.

It can be applied by authorities of different sizes, provided that there is sufficient political commitment and basic technical and financial capacity.

WHEN IS INTERNAL CONTRACTING MOST EFFECTIVE? Internal contracting delivers the greatest value when used as a multi-sectoral financing tool, supporting a portfolio of complementary actions rather than isolated investments. It performs best in contexts where assets are under direct LRA control and savings can be reliably measured and recovered.

Experience shows that its effectiveness is maximised when:

- Strong political commitment and senior management involvement enable a longer-term planning and implementation (beyond single project or annual budget cycles).
- Clear governance, monitoring, and repayment rules enable effective coordination across departments and service areas.
- Projects generate reliable and verifiable savings, whether in energy use, operational costs, or resource consumption.
- Actions are bundled across sectors or departments, combining high-return measures with smaller or longer-term interventions to balance financial performance and strategic impact.
- Savings are systematically reinvested, allowing the scheme to expand progressively across assets, services, or policy areas.

Under these conditions, internal contracting becomes a flexible and scalable model, supporting sustained energy and climate action while maximising the impact of public resources.

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