TITLE: THE DEVELOPMENT OF A NEW DISTRICT-WIDE INDOOR LEISURE CENTRE FACILITY, DOWNHAM ROAD, ELY

Committee: Corporate Governance & Finance Committee

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1.0 ISSUE

1.1 Development of a funding strategy to implement the new leisure centre facility.

2.0 RECOMMENDATION

2.1 Members are recommended to:-

2.2 To request that the Commercial Services Committee authorise Officers to proceed immediately with the procurement of an operator for the new leisure centre facility, and include within this the re-tendering for the management and operation of Paradise swimming until the opening of the new leisure centre.

2.3 To request that the Commercial Services Committee authorise Officers to secure the approval of funding from Sport England's Strategic facilities Fund

2.4 To request that the Commercial Services Committee agree their preferred facility mix for the leisure centre.

2.5 To task the Asset Development Committee with the identification of a programme of additional capital receipts to fund the leisure centre in 2015/16

2.6 To authorise the Corporate Unit Manager to bring forward proposals to Full Council for securing additional CIL contributions to fund the leisure centre

2.7 To instruct officers to review the certainty and timing of the capital receipts that are currently part funding the leisure centre as set out in the business plan for the design and build procurement

2.8 To request that the Financial Services Manager (S151 Officer) presents a further risk analysis to Corporate Governance & Finance Committee that will inform a prudential borrowing strategy.

3.0 BACKGROUND

3.1 TSC and AFLS&P Architects were appointed by the Council in June 2014, to complete a feasibility and options appraisal study for a new leisure centre, proposed for Downham Road in Ely. The study has been developed using the principle of being 'revenue neutral'. This means that not only will it need to address the current latent demands for sport facilities within the District, it will also need to cost the Council less ongoing revenue support than the current facility arrangements it replace. The Council currently has a budget allocation of £170,000 for the operation and management of Paradise Swimming Pool.

3.2 The Feasibility Study and Options Appraisal reflects a decision made by the project steering group on 26th August 2014 for TSC to focus more detailed work and sensitivity analysis on two preferred options; Option 5 and Option 6. This decision was made because TSC's appraisal work confirmed that Option 5 is the most affordable option and Option 6 best meets the identified strategic needs and requirements for indoor leisure facilities now and in the future for the District, but is the third most affordable option.

4.0 OPTIONS AND ISSUES

4.1 Capital cost estimates for all facility mix options have been set out in the Feasibility Study and Options Appraisal.

4.2 The key facility difference between these options in that Option 5 has a six lane swimming pool and option 6 has an eight lane swimming pool. The addition of 2 lanes of extra water space with an eight lane pool in Option 6 has a negative impact on both the upfront capital cost and also the long term income performance of the leisure centre, as swimming pools are a loss making element within the overall facility mix.

4.3 The estimated capital costs for options 5 and 6 are £11.834m and £12.696m respectively. The analysis of these costs together with secured and potential funding are set out in Appendix 1 to this report.

5.0 FINANCIAL IMPLICATIONS AND RISK ASSESSMENT

5.1 Prudential Borrowing Costs

(a) The CIPFA Prudential Code allows local authorities to borrow to finance capital expenditure, provided that such borrowing is **affordable**, **prudent** and **sustainable**. These factors are taken into consideration by the Council, when setting its Treasury Management Strategy each year for the next three years ahead. Risks and impacts of any potential borrowing is identified through a series of prudential indicators which highlight the risks exposed to the Council in terms of affordability, sustainability and prudence.

(b) The feasibility report on the proposed development identifies a prudential borrowing requirement of £6,488,352 for Option 5 and £6,377,151 for Option 6. Current assumptions are based on such borrowing being required to be undertaken in Quarter 3 of 2015.

(c) The resultant impact of such borrowing to the District Council would be the annual interest costs of financing the borrowing over the life of the loan combined with the statutory requirement to ensure the that prudent provision is made each year to set money aside from the revenue budget to cover the repayment of the loan. This is called the Minimum Revenue Provision, and the District Council sets its Minimum Revenue Provision policy each year, as part of the budget setting and treasury management strategy process. Members are then required to approve both aspects as part of the overall budget process.

(d) The feasibility study is based on an assumption of prudential borrowing for the sums set out above and borrowing for a period of 35 years. This would be matched to the estimated economic life of the new leisure facilities. Based on borrowing the sums quoted, the financial implications of the prudential borrowing would be as follows:-

	Annual Interest Costs	Annual Minimum Revenue Provision	Total Prudential Borrowing Costs
Option 5	£273,806	£185,381	£459,187
Option 6	£269,113	£182,204	£451,317

(e) The above interest costs are based on an assumption using current interest rate forecasts of borrowing for 35 years in Quarter 3 of 2015 at an interest rate of 4.22%.

(f) Whilst the above borrowing costs could be met from a combination of the current annual management fee for Paradise Pool (£170,000) and income receipts from the new leisure centre contractor (£289,187), there remains a funding gap of £1.530m for option 5 and £2.500m for option 6. If the Council were to take out additional long term borrowing to meet this gap, there would be additional revenue costs of:

	Annual Interest Costs	Annual Minimum Revenue Provision	Total Prudential Borrowing Costs
Option 5	£64,566	£43,714	£108,280
Option 6	£105,500	£71,429	£176,929

The total estimated annual costs of borrowing for both of the options would therefore be:

	Annual Interest Costs	Annual Minimum Revenue Provision	Total Prudential Borrowing Costs
Option 5	£338,372	£229,095	£567,467
Option 6	£374,613	£253,633	£628,246

The total costs to the Council over the 35 year loan period would be:

Option 5 - £19,861,345

Option 6 - £21,988,610

Clearly, if the funding gap could be financed from either capital receipts and / or CIL monies, the additional interest and MRP would not be incurred.

5.2 <u>Risk Assessment</u>

(a) It is, however, vital that a number of important risk factors are taken into account when considering the affordability, prudence and sustainability of borrowing such significant sums. These risks include:-

- An assumption that the level of income forecast from the new facility will be sufficiently high enough to finance the costs highlighted above. Any shortfall in income would place financial pressures on the Council in terms of its ability to fully finance the borrowing costs highlighted above. Although the Feasibility Study and Options Appraisal shows that the Council could expect income from the operator of £0.285m and £0.278m per year for options 5 and 6 respectively, this has yet to be market tested.

- An assumption that all of the identified “other funding” sources will be successfully achieved and thus any prudential borrowing required will be restricted to the sums required above under options 5 and 6. Currently there is only £0.579m of secured funding for the leisure centre. There are risks attached to the certainty of the amount and / or timing of some sources of funding. These include certain capital receipts, the contribution from the cinema development, the Sport England and Football Foundation grants and the 2015/16 New Homes Bonus.

- An assumption that the timing of the projected cash outflows and inflows will be in accordance with current expectations;

- An assumption that interest rate expectations remain within their current forecast levels between now and when the borrowing is required. Any increase in interest costs due to economic factors between now and when the borrowing is required will expose the District Council to potentially significant interest rate risk until such time as the borrowing is secured. A change in interest rate expectations would cost the Council an additional £20,046 per annum for the life of the borrowing on top of the figures quoted above, if interest rates were to rise by 0.25% between now and 2015.

- There are cash flow timing issues with regard to the prudential borrowing that is required to part fund the leisure centre and the savings from the closure of Paradise Pool and the receipt of income from the new facility, both of which will be used to fund the borrowing costs of either £6.488m (option 5) or £6.377m (option 6). The Council would therefore need to identify how it can fund what in effect will be a ‘bridging loan’ until such time that the new leisure centre produces an income stream and the Paradise Pool is closed.

- There are additional costs associated with both options for which the funding source is yet to be determined. These are £1.5m for option 5 and £2.5m for option 6. The use of capital receipts might be a cheaper option to the Council than taking up additional long term borrowing as there won’t be any financing costs associated with this approach. On the other hand, the use of internal borrowing would reduce the interest earned on investing the Council’s surplus cash flow.

- The affordability of this significant capital project needs to be considered within the context of the Council’s overall forecast financial position over the medium term. Currently the financial forecasts indicate that the Council is likely to face budget pressures in 2016/17 of £1.8m and £2.5m in 2017/18. It is crucial that the affordability of the proposed leisure centre is not considered in isolation, but alongside the wider financial challenges facing the Council. In particular that Central Government funding is set to reduce further through to

2019/20 and there is a lack of certainty of the continuation of New Homes Bonus (76% of which is funding the Council's base budget).

(b) Having highlighted the risks above, there are a number of possible steps the Council can take to manage and mitigate such risks. These include:-

- Phasing the borrowing over a period of time, rather than borrowing in one lump sum, to match the expected cash-flows over the life of the project build. This would help defer borrowing costs and match the timing of any borrowing to the cash-flows of the project, but would expose the Council to further potential interest rate risk, if borrowing costs were to rise in the latter part of 2015 and into 2016;

- Capitalising interest costs, so that the costs associated with borrowing prior to the commencement of the project are deferred and added to the overall project costs. This would reduce interest costs in the early years, but potentially require a larger sum to be borrowed over the life of the project. This would need to be balanced against the estimated income levels arising from the new leisure centre.

- Undertaking "forward borrowing" whereby prudential borrowing is agreed with a potential lender at an agreed rate ahead of the need of the borrowing (up to 2 years in advance). This reduces the risk to the Council of interest rate risk, but a "premium" is likely to be added to the borrowing costs to offset the certainty element.

(c) The District Council is working alongside its treasury management advisors, in forecasting the potential economic outlook, identifying the potential impact on borrowing interest costs and establishing the most prudent form of borrowing to finance the new facilities.

6.0 ARGUMENTS AND CONCLUSIONS

6.1 TSC's work has helped to clarify the financial implications to the Council of implementing a range of facility mix options within a new leisure centre facility. Focussing on the two preferred options that were assessed in more detail indicates that Option 5 is cheaper to build and has better viability from an income generation point of view, than Option 6. However, Option 6 will best meet the identified strategic need for indoor leisure facilities and future growth requirements up to 2026.

6.2 A detailed risk register will now be completed for the project at the next stage of work. However, there are a number of risks at this high level business planning stage, which have been identified in this report and which now need to be given further consideration.

7.0 EQUALITY IMPACT ASSESSMENT

Not required at this stage.

8.0 APPENDICES

Appendix 1 - Cash Flow Projections For Options 5 and 6 (Exempt)

Background Documents	Location	Contact Officer
	Room 206 The Grange Ely	Linda Grinnell Financial Services Manager (S151 Officer) 01353 616470 linda.grinnell@eastcambs.gov.uk