AGENDA ITEM NO 8

NEW DISTRICT LEISURE CENTRE – FUNDING STRATEGY

Committee: Council

Date: 28th June 2016

Author: Director, Resources

[R43]

1.0 ISSUE

1.1 To approve the funding strategy for the new district leisure centre.

2.0 RECOMMENDATION(S)

2.1 It is recommended that:

a) the funding strategy be approved;
b) the revised capital programme and Treasury Management Strategy be approved;
c) the further engagement of MACE as project manager;
d) the Council submits an Efficiency Plan to DCLG; and
e) the revised Medium Term Financial Strategy be noted

3.0 BACKGROUND

3.1 At its meeting of 22nd October 2015, Council resolved to:

a) Approve the programme timetable;

b) Approve the allocation of up to £500,000 within the capital programme to progress the project to RIBA Stage 4 and the procurement of the contractor and operator;

c) Reflect the amendment to the capital programme into the mid-year review of the Council's Treasury Management Strategy;

d) Instruct the Chief Financial Officer to bring forward a further report to Council in April 2016 detailing the outcome of the procurement of the contractor and a recommended funding strategy to progress the project to completion.

3.2 The programme to deliver a new leisure centre has delivered the next steps as resolved above, including the recommendation to appoint a building contractor and operator elsewhere on the agenda.

3.3 This report provides the Funding Strategy to enable the project to progress through to completion.

4.0 CAPITAL PROGRAMME

4.1 The overall project costs for the development are projected to be £13.5 million. This capital budget is as follows:

Cost Heading	Project Budget	Final Projection
Construction	£11,790,000	£11,776,119*
Design/Project Fees	£1,360,000	£1,360,000
ECDC Contingency	£350,000	£363,249
Total	**£13,500,000**	**£13,499,368**
Option to Fund Operator Fit-out		£441,597
Total Capital Expenditure		**£13,940,965**

* The Construction costs include the guarantee that the Constructor will deliver "Value Management" cost reductions of £332,184. If this guarantee is not met, then the ECDC Contingency budget would be removed.

4.2 The tender costs match those of the project budget, giving confidence that the estimates given throughout the project are realistic and robust. Details of the construction work are provided in a separate report on your agenda.

4.3 The majority of Design/Project Fees relate to the work commissioned to MACE to deliver. The Council appointed MACE in October 2015 and released funding to take the Council to its current stage. MACE has updated its proposal, but retained the cost within that previously reported to Council, through to completion of the project. The updated proposal is attached at Appendix A as an exempt appendix to this report.

4.4 There are advantages in the Council funding the fit-out costs which are the responsibility of the operator. This would mean the Council funding these capital costs, but seeing an increase in the operator profit.

4.5 The capital programme also includes a provision of £200,000 to cover anticipated costs relating to the broader site, for example potential draining and other infrastructure works.

4.6 The project has always been assumed to be funded through a combination of internal funds (primarily capital receipts and CIL); Sport England grant; and the remainder being through Prudential Borrowing.

4.7 The assumed funding of the capital costs set out in para 4.1 is:

Funding Source	
Capital Receipts	£1,817,291
Community Infrastructure Levy	£606,000
Sport England	£1,500,000
Prudential Borrowing	£10,017,674

Total	£13,940,965

In addition to the above, prudential borrowing of £200,000 has been assumed to cover the costs shown in paragraph 4.5. It is anticipated that further funding from other sources, e.g. capital receipts, will come forward to reduce this borrowing.

4.8 The capital receipts include those currently held but unallocated; future capital receipts assumed in FY2016/17 to 2017/18- including the deferred capital receipt from the sale of Barton Road. There is a marginal risk here, that the capital receipt from Barton Road is not available in sufficient time. No provision has been made around any capital costs or potential proceeds from the Paradise Pool site.

4.9 The Community Infrastructure Levy uses the proportion previously approved by full Council, of CIL already received and assumed to be received in FY2016/17. It has been assumed that no further CIL is made available to fund the capital programme in FY2017/18.

4.10 The Sport England funding is dependent on a successful grant application. This application will be made immediately after Council, and it is anticipated that the outcome will be known by September 2016. If funding is not received at the level projected, options will need to be evaluated and a further report brought back to full Council in the autumn. At this stage, without full Sport England funding, the project would be unaffordable and would therefore have to be redesigned, which will create a significant delay as the project will need to be redefined and refinanced.

4.10 A revised capital programme and funding plan is attached at Appendix B.

5.0 <u>TREASURY MANAGEMENT STRATEGY</u>

5.1 The remainder of the capital funding will be from Prudential Borrowing. The Council has already approved the use of Prudential Borrowing to loan fund up to £5 million for the Trading Company. The use of Prudential Borrowing to part fund the Leisure Centre of £10 million would increase the Council's overall borrowing requirement to £15 million.

5.2 Prudential Borrowing is permitted where the use of borrowing to fund capital expenditure is prudent. Reflecting on the risks, the Council's financial position, and future Medium Term Financial Strategy and future capital plans; the Council can raise borrowing as source of funding.

5.3 The Council has a fully funded Capital Programme; it has a Medium Term Financial Strategy which is largely funded (accepting that receiving a commitment from DCLG on future grant support would assist significantly); healthy cash balances (currently circa £24 million) and a reputation for delivering year on year efficiency savings and income growth; then in my view, undertaking new borrowing to fund the leisure centre is both prudent and affordable.

5.4 The capital costs of the leisure centre are robust and realistic (ref para 4.2) and the funding is all in place (with the exception of Barton Road and Sport England funding). The former is in the control of the Council and is considered a minimal risk. Reduction or loss of either funding stream would however entail a review of the funding strategy and it is not clear at this stage that the gap would be affordable.

5.5 There is a requirement to revise the Council's Treasury Management Strategy- which is attached at Appendix B. This shows the treasury implications in funding both the Trading Company and Leisure Centre (in part) from Prudential Borrowing. The strategy remains as approved in February 2016 ie continue to make short term, deposits with surplus cash, ensuring cash is available to support the needs of the capital programme (which will now include the Leisure Centre).

5.6 With cash balances being circa £24 million; funding the existing capital programme, the use of reserves to support the MTFS, the Council has sufficient cash balances to avoid the need to externally borrow. This means that the interest costs of the prudential borrowing are the loss of investment interest on cash balances (around 1%)- rather than the costs of external borrowing) interest rates (currently 2.70%).

5.7 Regardless of whether Prudential Borrowing is internally or externally financed, the Council is required to set aside a revenue charge- the Minimum Revenue Provision- which is in effect the repayment of the "Principal" element of the borrowing. The level of revenue charge depends on the Council's policy, which it is to spread the repayments over the expected life of the asset. Typically, this would be around 35 years for an asset such as a leisure centre. However, to ensure the Council is acting prudently, I would advocate commencing with a period of 25 years (and a period of 10 years for the fit-out costs). The 25 year period is primarily due to the risk that the operator profit on a brand new facility will be greater than on an older facility, so when the operator contract is retendered in 12 years time, the profit may be lower- and as such the Council may wish to extend its remaining borrowing repayment over a 35 year time at some future date. This will allow the Council to remain prudent throughout the life of the leisure centre, and enable it to remain cost neutral on the revenue budget.

5.8 As the project will be repaying its loan over 25 years, then over that time cash balances will increase by £10 million. In effect, at year 25 the Council will have an asset of the leisure centre, fully funded. This clearly increases the Council's asset base in its balance sheet.

5.9 The annual revenue cost of the prudential borrowing of £10 million is £537,380. Of this sum, £488,804 is the level of revenue cost for the 25 year period which needs to be met.

6.0 REVENUE IMPLICATIONS

6.1 The revenue implications from the leisure centre will be incorporated into the Council's Medium Term Financial Strategy and in future, annual budgets. It has been assumed that the impact from the construction and operation of the leisure centre will be cost neutral.

6.2 The main cost is the repayment of the loan (ref para 5.9). In addition, there will be incidental costs around insurance, grounds maintenance etc.

6.3 As referred to in para 5.7 above, it is critical that the Council maintains and protects the value of the leisure centre- both in terms of its future usage by the community, but also to ensure that the contractor is able to operate the facility at a profit in the future. As the Council will retain responsibility for replacing key infrastructure to the leisure centre (eg plant); also be responsible for the fabric of the building and need to undertake a "refresh" to the leisure centre (suggest after 10 years), then the Council must ensure it has sufficient resource in place. The overall costs of these issues over a 25 year asset life have been estimated at £5 million; and a revenue provision will be made to a "Sinking Fund" for such spend.

6.4 The operator profit is set out in the separate report on the appointment of the operator. The figure shown is an average over the 12 years of the contract. In the first two years of operation, there is no operator profit. This is due to the upfront costs of ICT systems, training, and marketing to generate the income. In the subsequent 10 years of the contract, the operator profit is in line, and generally exceeds, the average profit figure.

6.5 In addition, the closure of Paradise Pool will deliver an annual saving to the Council of £170,000 per annum.

6.6 The revenue implications from each of the above issues are shown at Appendix D. These show that in the first two years there is a funding gap. It is suggested that this be met from the Council's New Homes Bonus Reserve (which had previously been allocated to fund the project costs of the leisure centre). This approach will enable the revenue implications of the leisure centre to be cost neutral to the Council.

6.7 No allowance has been made for any surplus profit share, should the operator deliver a greater profit than has been assumed; nor the potential opportunities in working with the operator to ensure that the final contractual agreements for both parties are financially efficient.

7.0 EFFICIENCY PLAN

7.1 Although the impact of the leisure centre on the Council's Medium Term Financial Strategy is cost neutral, the Council is increasing its risk exposure. The variables contained in the Council's MTFS are generally upward ie business rates continue to increase, the efficiency savings being made year on year exceed the target. However, the Council does face a period of uncertainty with regard to the pace of reductions in Revenue Support Grant (RSG). A revised MTFS incorporating the outturn position from FY 2015/16 and the leisure centre is attached at Appendix E.

7.2 The outturn is being reported to the Corporate Governance and Finance Committee at its meeting on 30th June 2016. The revenue underspend in FY2015/16 has lead to an increase in the Council's Surplus Savings Reserve. There remains a small budget deficit projected in FY 2018/19 of £271,291; which increases significantly in the following years. The Council therefore has time in which it can identify further savings and income opportunities to close the budget deficit for FY2018/19 and the challenges of subsequent years.

7.3 The DCLG has invited local authorities to submit an Efficiency Plan, in exchange for obtaining assurances that the grant settlement offered by DCLG in February 2016, which covers the financial years 2016/17 to 2019/20, are honoured. Due to the increased risks around the Council's finances, it would be prudent to secure some certainty around RSG allocations. I therefore recommend the Council to submit an Efficiency Plan to DCLG to secure the 4 year settlement.

7.4 The Council's Financial Strategy to deliver a year on year balanced budget is twofold:

- Continue to identify and drive efficiency savings: The Council has a strong track record in delivering significant savings. In addition, members have recently approved a Transformation Programme

  http://www.eastcambs.gov.uk/sites/default/files/agendas/tp120516_Q263.pdf

  which identifies financial savings. This Programme is being implemented, with regular updates into the Transformation Sub-Committee.

- Drive a broader commercial agenda: A full business case was approved by Council in January 2016

  http://www.eastcambs.gov.uk/sites/default/files/agendas/fc070116_Q158_Ap1.pdf

8.0 CONCLUSIONS

8.1 The leisure centre project can be delivered "cost neutral". It has a number of risks, which are set out in the report, and a significant level of prudence has been adopted to these risks. The project is large to East Cambs District Council, and securing certainty over future grant levels will provide a reduced risk to the Council's Medium Term Financial Strategy.

9.0 FINANCIAL IMPLICATIONS

9.1 The financial implications are shown in the revised Capital Programme, Treasury Management Strategy and Medium Term Financial Strategy.

10.0 APPENDICES

10.1 Appendix A – Revised Capital Programme
Appendix B - MACE Management Proposal (Exempt Appendix)
Appendix C – Revised Treasury Management Strategy
Appendix D – Leisure- Revenue Implications
Appendix E - Revised Medium Term Financial Strategy

Background Documents	**Location**	**Contact Officer**
Report to Council- 22nd October 2015- “Procurement of a District Leisure Centre” Report to Council- 7th January 2016- “Establishment of the Local Authority Trading Company” Report to Council- 25th February 2016- “Revenue Budget, Capital Programme and Council Tax 2016/17” Report to Transformation Sub-Committee- 12th May 2016- “Review of the Transformation Programme and ICT Service”	Room 105, The Grange, Ely	Andy Radford Director, Resources (01353) 616303 E-mail: andy.radford@eastcambs.gov.uk