

IN-SOURCING LEISURE PROVISION

Cabinet Member for Leisure and Parks

Date: 14 February 2023
Agenda Item: 10
Contact Officer: Simon Fletcher, Chief Executive, Anthony Thomas, Assistant Director Finance & Commissioning and S151 Officer, John Smith, Performance & Programmes Manager, Sarah Sleigh, People Policy Officer

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CABINET

Key Decision? YES

Local Ward Members All Wards.

1. Executive Summary

- 1.1 The council has been approached by Freedom Leisure to agree a termination of the Leisure Operating Contract with them on 1 April 2023. The request follows several months of ongoing discussion and negotiation about the future of the contract in response to Freedom's requests for further financial support over the coming two financial years, as a result of the energy price increases.
- 1.2 The paper proposes a mutually agreed termination of the Leisure Operating Contract with Freedom Leisure and, subsequently, the transfer of the management and operation of the council's leisure portfolio (comprising Burntwood Leisure Centre and Friary Grange Leisure Centre) to Lichfield West Midlands Traded Services (LWMTS), the Council's wholly owned company.

2. Recommendations

- 2.1 Cabinet approve and recommend to full Council a mutually agreed termination of the Leisure Operating Contract with Freedom Leisure.
- 2.2 Cabinet approve the transfer of the management, budget, and operation of the council's leisure portfolio (comprising Burntwood Leisure Centre and Friary Grange Leisure Centre) to the Council's wholly owned company / new organisational structure as appropriate with the Company assuming responsibility for paying the contract commercial bid and contracted indexing to the Council from 1 April 2023 to 31 December 2027 as detailed in the financial implications section.
- 2.3 Cabinet approve and recommend to full Council that the payment received from Freedom Leisure (as set out in paragraph 2.3 of the confidential report) be set aside in an earmarked reserve held by the Council to cover additional costs of energy supply in 2023/24 and 2024/25 within the wholly owned company / new organisational structure and thereafter revert to General Reserves.
- 2.4 Cabinet delegate authority to the Cabinet Member for Parks and Leisure and the Chief Executive in consultation with the Monitoring Officer to negotiate and agree any agreements necessary to complete the transfer subject to them being within Approved Budgets.

3. Background

- 3.1 In July 2015, the council commissioned FMG Consulting to undertake an options appraisal for the management of the council's leisure centres and services. As well as ensuring that the council has a leisure service that is fit for the future, the review was also tasked to deliver a budget reduction of at least £200,000 per year.
- 3.2 In March 2016, Cabinet agreed to the principle of outsourcing the management and operation of Burntwood and Friary Grange leisure centres, as a means to ensuring both a fit for the future service and the necessary budget savings, and to seek proposals to appoint a project manager to progress this work.
- 3.3 In July 2016 and following a formal tendering process for the project manager, a contract was awarded to Max Associates Ltd, to progress with the outsourcing of the council's leisure centres. Following a further competitive process, the Council appointed Freedom Leisure to manage and operate its leisure portfolio comprising Burntwood Leisure Centre and Friary Grange Leisure Centre, pursuant to a Leisure Operating Contract dated 1 February 2018. The contract period is for 10 years with an option to extend by a period of 5 years.
- 3.4 Clause 29 of the Contract recognised the long-term future of Friary Grange Leisure Centre was subject to ongoing discussions between Staffordshire County Council and Friary School. The Contract therefore provided for partial termination in relation to Friary Grange Leisure Centre.
- 3.5 Despite ongoing discussions between the parties, Staffordshire County Council and Friary School were unable to commit to the long-term future of Friary Grange Leisure Centre. The Council, therefore, exercised its rights, pursuant to Clause 30.1(a) of the Contract to partially terminate the Contract in relation to Friary Grange Leisure Centre, when it made its decision to close the facility in March 2019.
- 3.6 After the Notice to Terminate was served, there was a huge community response to the news. Members, customers and clubs raised the issue through social media, a community meeting, a petition and through contact with the council, showing how strongly they felt about having access to a leisure centre and swimming pool in Lichfield city. As a result, partners, including the county council and school, committed to explore a range of potential options to address the immediate threat of closure, as well as looking at future options for more sustainable leisure provision in the district. A special cabinet meeting on the 7 October 2019 was held at the Garrick Theatre. A cabinet debate took place following the public speaking session, where it voted to recommend (to Full Council) keeping the leisure centre open and investing £695,000 in repairs and maintenance. Cabinet also recommended amending the council's financial plan to add £5million into the capital programme to help future leisure facilities in Lichfield. An interim position was agreed for Freedom Leisure to continue to manage and operate Friary Grange Leisure Centre, subject to adjustments to the contract set out in a Deed of Variation dated 22 June 2020.
- 3.7 This Deed of Variation deals only with the agreed variations relating to the management and operation of Friary Grange Leisure Centre arising from the new arrangements between Staffordshire County Council, Friary School and the Council and specifically the exclusion of the sports hall, all weather pitches and dance studio from community use for the remainder of the Contract Period (as defined in the Contract). It also set out that the annual payment payable by the Council to Freedom Leisure be adjusted on an annual basis by an increase of £63,750 for the financial year 1 and by £85,000 for each subsequent financial year commencing on 1 April, in compensation for the loss of revenue arising directly from the removal of these facilities.
- 3.8 The contract with Freedom Leisure has now been in place for five years. During this period Freedom has successfully delivered a £1.1m capital programme (funded by LDC through borrowing) for Burntwood leisure centre, in 2019. This included a refurbishment of the ground floor consisting of a new reception/café area and new aerobics studio. The first floor area was redesigned to increase the size of the gym provision, including a functional training zone and designated spin room.

- 3.9 From the initiation of the contract the council developed a partnership approach with Freedom Leisure to deliver leisure services. Further details of this can be found in the confidential version of this report.

Covid

- 3.10 In response to the Health Protection (Business Closure – Coronavirus) (England) Regulations 2020, Freedom Leisure closed the leisure centres to prevent the spread of Covid-19 in March 2020. This closure had a significant and immediate impact upon the revenue generated by the facilities and meant Freedom Leisure were unable to both meet the costs of running the centres or pay the Council their contractual annual payment.
- 3.11 Following Government guidance PPN 02/20 and PPN 04/20 and sector specific guidance, on 3 April 2020, the Council agreed a package of financial and other support measures to help mitigate the impact of Covid-19 on Freedom Leisure. The Council agreed a short-term package of financial and other support measures, time limited, until 30 June 2020.
- 3.12 As the Covid Pandemic continued it was evident a temporary closure of leisure facilities was not sufficient, and the Government began to introduce UK wide and sector wide lockdowns. Which meant that leisure centres would remain closed for an extended period. The Council agreed a further package of financial and other support measures, to support Freedom Leisure in August 2020. This, again, was time limited until the end of March 2021. The financial package and other support measures set out in the second Deed of Variation were subject to Open Book Interim Data provided by Freedom Leisure.
- 3.13 As the country exited Covid, Government issued a 'Road Map' for the easing of Covid-19 Restrictions and the re-opening of leisure facilities. In accordance with the Road Map, Freedom Leisure was permitted to open all Indoor Facilities on 12 April 2021 and Outdoor Facilities on 17 May 2021, with some social distancing measures remaining in place until 21 June 2021. The Council and Freedom Leisure agreed a 're-opening schedule' to ensure that all facilities were fully opened. We also agreed a further package of financial and other support measures. This was time limited and expired on 30 June 2021. The Council confirmed its intention to withdraw all reliefs from all third-party contractors, including Freedom Leisure after 1 July 2021. Freedom Leisure acknowledged that any support measures were entirely at the discretion of the Council and that there would be no extension to the third and final support measures.
- 3.14 In return for the Council making this funding available, Freedom Leisure agreed to comply with the provisions and obligations of the funding agreement as if it were a party to it in place of the Council, including the obligations for repayment of the funding. This was completed by way of a Deed of Indemnity Agreement.
- 3.15 Freedom Leisure acknowledged the principles set out in PPN 02/20 and PPN 04/20 which required them to act in good faith with regards to requests for support measures and to take all reasonable steps to exit from such measures and resume full service delivery in accordance with the Contract including resumption of payment of the Annual Payment to the Council.
- 3.17 Since the Covid Lockdowns, both leisure centres have recovered reasonably well, although some income generating activities have not reached pre covid levels, including casual swimming and fitness memberships, which are currently operating at around 80% when compared to active memberships in early 2020. In other areas such as learn to swim and fitness classes the demand has increased at both facilities.

Cost of living crisis

- 3.17 Nationally, almost half of adults say that they have less disposable income today compared to a year ago.

- 2 in 5 (40%) people said the cost of living increase was having a ‘negative impact’ on their ability to be active in August 2022, up from a third of people in March 2022 (an increase of 6.7%)
- Almost half of people (48%) think the cost-of living is likely to have a negative impact on their ability to be physically active in the future.

3.18 In July 2022, Freedom Leisure provided a report outlining the challenges being faced by the Leisure Partnership Contract. This included wage inflation, increased cost of supplies, equipment, goods and services and energy price rises. The report requested the Council provide full financial support to meet the impact of the energy price increase. (As set out in the confidential report)

3.19 The council sought legal advice from Winckworth Sherwood as set out in paragraph 3.18 of the confidential report.

3.20 In September 2022, Freedom Leisure provided a report containing their latest local energy price increase predictions. The report also contained an options appraisal (set out in paragraph 3.19 of the confidential report together with other considerations).

Proposal

3.21 The Chief Executive, in consultation with the Cabinet Lead for Leisure, and the Leader of the Council, has led subsequent discussions and negotiations with Freedom Leisure since late 2022. Both Councillors’ steer was clear; the Council cannot support Freedom Leisure financially any further than has already been provided, but also will not countenance a closure of any part of either the Lichfield or Burntwood facilities.

3.22 In December 2022, following repeated requests for the Council to reconsider its position on financial support and the part / full closure of some of the facilities in the district, and recognition the Council would not concede on either of these points and instead expected Freedom Leisure to fulfil its contractual obligations, both parties agreed to begin (without prejudice) negotiations over a mutual termination of the contract.

3.23 The outcome of those negotiations is that:

- Both parties agree a mutual termination of the remaining period of the contract
- Freedom Leisure will pay the council an early exit fee (detailed in the confidential report)
- Freedom Leisure’s payment will be made in two instalments with two thirds paid on termination (1 April) and the remainder six months later (1 October)
- Both parties agree a communications strategy to support the announcement of a termination of the contract.

3.24 Cabinet is requested to consider, approve and recommend to Full Council this proposal and the negotiated terms of exit for Freedom Leisure with effect from 1 April 2023 (or as soon as possible thereafter).

Alternative Options	<ol style="list-style-type: none"> 1. Cabinet could decide not to transfer the leisure operating contract into the LWMTS and to continue to hold Freedom Leisure to account in respect to the existing leisure outsource contract. Freedom Leisure have continued to implement cost cutting options, despite the council's objections and this is likely to continue leaving the facilities with higher charges, fewer staff, less health and wellbeing activities, smaller timetables, reduced opening times and the potential removal of higher cost facilities such as the health suite. This impairs the council's ability to support its community and we could end up with facilities that are open less frequently and become less affordable to those in most need in our community.
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2. The council revisit the leisure market and seek tenders from leisure operators to take over the contract. This could take between 12-18 months and is unlikely to provide any betterment to the existing leisure contract due to it being based on financial performance. The leisure market is slowly recovering from the effects of the COVID 19 pandemic and are facing challenges such as the cost of living crisis and high fuel costs meaning that appetite from the market to take on new commercial contracts is slim unless the financial risks are either shared, or more likely fully sit with the local authority.

Consultation

1. There will be public engagement and communication process as part of any changes to the operational management of the leisure centres. Overview & Scrutiny Committee was consulted at their Special meeting on the 8th February 2023 and their views will be reported directly at the Cabinet meeting.

Financial Implications

The Commercial Bid from Freedom Leisure assumed payments from the Council in the first three years of the 10 year contract (2017/18 to 2019/20) and then income to the Council from 2020/21 onwards.

However during COVID-19, financial support was provided to Freedom Leisure including foregoing some or all of the commercial bid income due to the Council in 2020/21 and 2021/22:

Commercial Bid Foregone	£142,778
Financial Support	£425,005
Business Rates & Grants	£63,486
Total Support	£631,269
National Leisure Recovery Fund	(£224,418)
Public Sector Support	£406,851

To inform the negotiations with Freedom Leisure a range of financial projections were modelled using different assumptions from the budgeted Council commercial Bid to the Freedom's Commercial Bid plus Total COVID-19 support plus the projected costs of transition.

The Budgets included in the Approved Medium Term Financial Strategy related to the Freedom Leisure Commercial Bid are shown in detail at **APPENDIX A** of the confidential report (and in summary in the financial implications of the confidential report).

The commercial bid figures provided by Freedom Leisure as part of the procurement in 2017/18 will have been negatively impacted by events over the last three years. Therefore the current operating costs and income projections have been requested from Freedom Leisure as part of the due diligence process. However it is likely that energy costs and income will not be performing in line with budgets.

There are also a number of other financial implications for the Council and LWMTS that will need to be considered as the project progresses:

- In terms of any charges for services to or from the Council, the Council and Company must be mindful of transfer pricing requirements and therefore the actual approach to pricing to be adopted will need to be developed in consultation with the Council's Tax advisors
- There are pension implications for both the Council and wholly owned company / new organisational structure. The wholly owned company / new organisational structure will be classed as a designated body and would be admitted into the scheme following a Company resolution to join. This involves TUPE transfers of staff from Freedom Leisure and the wholly owned company / new organisational structure becomes a new participating Fund employer for and transferring employees remain eligible for LGPS

	<p>membership and contributions under the Best Value Guarantee. The arrangement with Freedom leisure utilises a “pass through” arrangement. Under this option the wholly owned company / new organisational structure would pay a fixed contribution rate (Freedom Leisure pay 26.5%) throughout its participation in the Fund and on cessation does not pay any deficit nor receive an exit credit. In other words, the pensions risks “pass through” to the Council and an earmarked reserve has been established to mitigate the risk. In 2022/23 the total contribution rate is 30.1% although this could change under the new Local Government Pension valuation from 1 April 2023.</p> <ul style="list-style-type: none"> The Company’s Business Plan is subject to approval by the Council on an annual basis or if material changes are proposed during the financial year to ensure proposed activity is transparent and has shareholder approval.
Approved by Section 151 Officer	Yes
Legal Implications	1. Solicitors have been appointed to ensure that the council has the most appropriate legal advice as part of this proposal and to ensure that’s its protected contractually throughout any transition process.
Approved by Monitoring Officer	Yes
Contribution to the Delivery of the Strategic Plan	1. The transition of the operating contract from one operator to another will contribute to our strategic objective of creating a healthy and safe community . By retaining these services, it will increase the number of people within the district who are physically active.
Equality, Diversity and Human Rights Implications	1. Providing accessible local leisure facilities can help encourage those that would most benefit, to be more active, more often. Such individuals may have protected characteristics including age, gender and disability or ill-health. The key driver to changing the facilities operator is to ensure that there’s no reduction in the timetabling of health and wellbeing activities, opening times, and facilities within the centres.
Crime & Safety Issues	1. As the project moves through the operator transition phase, these elements will be considered further to ensure the new operator is aware of any community safety and crime challenges at both sites and to ensure that they play a positive role in the reduction of crime and improvement of safety.
Environmental Impact	<p>1. The operational transition from one organisation to another should see no negative environmental impact.</p> <p>2. There is an opportunity to ensure that any new contracts procured through the LWMTS are more locally sourced and that organisations providing these new services are also signed up to carbon offsetting promises.</p>
GDPR / Privacy Impact Assessment	1. Data processing arrangements will be addressed as part of any transition from one operator to another.

	Risk Description & Risk Owner	Original Score (RYG)	How We Manage It	Current Score (RYG)
A	There's likely to be several operational risks associated with the transition from one operator to another such as the provision of goods and services, IT networks and routine management and maintenance contracts.	Likelihood: Yellow Impact: Red Score: Yellow	A detailed Risk Log linked to the operational transition will be developed in collaboration between LDC, Freedom Leisure and the LWMTS to ensure these are mitigated.	Likelihood: Green Impact: Yellow Score: Yellow
B	Freedom Leisure don't cooperate with the 'transfer of operations' to the LWMTS	Likelihood: Yellow Impact: Yellow Score: Yellow	Financial agreements and legal documents agreed and signed beforehand to ensure that there's a collaborative approach. The current Leisure Operating Contract makes a provision for this.	Likelihood: Green Impact: Yellow Score: Yellow
C	Legal requirements need to be in place for contract termination with Freedom Leisure and any new contract with LWMTS.	Likelihood: Yellow Impact: Yellow Score: Yellow	DWF solicitors have been appointed to ensure that all legals are dealt with appropriately.	Likelihood: Green Impact: Yellow Score: Yellow
D	LDC and the LWMTS having the appropriate resource to manage the transfer and ensuring service delivery.	Likelihood: Yellow Impact: Yellow Score: Yellow	Provision is being made for sufficient support from HR/Legal/Finance/ Communications during the management of the transfer into the LWMTS and bedding in of a new leisure contract.	Likelihood: Green Impact: Yellow Score: Yellow
E	Negative reaction from employees and customers to the transition.	Likelihood: Yellow Impact: Red Score: Yellow	Ensure that an effective communications plan is prepared and implemented.	Likelihood: Green Impact: Yellow Score: Yellow
F	The LWMTS not delivering on the proposals within any new operating contract.	Likelihood: Yellow Impact: Red Score: Yellow	A detailed contract and service specification will be drafted which the LWMTS will have to agree to.	Likelihood: Green Impact: Yellow Score: Yellow
G	The requirement to ensure value for money and associated service delivery.	Likelihood: Yellow Impact: Yellow Score: Yellow	To ensure that the LWMTS is given a substantial contract period to enable them to operate the facility.	Likelihood: Green Impact: Yellow Score: Yellow
H	Data Protection challenges, data sets between organisations being shared.	Likelihood: Yellow Impact: Yellow Score: Yellow	GDPR processes in place to ensure that any data sets that can be shared are, and those which can't to remain the property of the primary organisation.	Likelihood: Green Impact: Yellow Score: Yellow
I	Staff unaware of the transition or challenge the process.	Likelihood: Yellow Impact: Yellow Score: Yellow	Ensure that a strong consultation and engagement process is in place specifically for employees and that a robust TUPE process is followed	Likelihood: Green Impact: Yellow Score: Yellow
J	The council need to ensure that once the LWMTS takes over the operations of the Leisure facilities, they are run day to day in an acceptable manner.	Likelihood: Yellow Impact: Yellow Score: Yellow	Governance arrangements to be agreed with by both partners and implemented as part of future monitoring and management arrangements.	Likelihood: Green Impact: Yellow Score: Yellow
K	Pension risks including admitted body status	Likelihood: Yellow Impact: Red Score: Red	Legal and Pension Fund advice in relation to TUPE and admission requirements.	Likelihood: Yellow Impact: Yellow Score: Yellow
L	The Council breaches its partial exemption limit and is unable to reclaim VAT of c£100k per annum related to exempt activities in relation to this option together with the new	Likelihood – Red Impact -Red Risk - Red	Financial modelling will need to be undertaken based around the level of exempt income such as football pitchchires utilising the series of lets exemption etc. and advice sought from the Council's VAT advisor on the level of risk and options to manage any risk.	Likelihood – Yellow Impact - Yellow Risk - Yellow

	leisure centre and the CIL investment			
M	The Company breaches the 20% TEKKAL exemption due to the external income of (£425k) per annum	Likelihood – Red Impact -Red Risk - Red	Legal advice will be procured and financial modelling based on the approved Business Plan and known plans has been undertaken.	Likelihood – Yellow Impact - Yellow Risk - Yellow
N	The commercial bid contribution is not paid to the Council or financial support is required due to adverse financial performance	Likelihood – Red Impact -Yellow Risk - Red	An allowance is included in the Minimum Level of Reserves for adverse leisure centres contract performance.	Likelihood – Yellow Impact -Yellow Risk - Yellow
O	The new insurance contract does not include cover for leisure centre management	Likelihood – Red Impact -Red Risk - Red	Early engagement with the new insurance provider to determine insurance requirements and potential cover.	Likelihood – Yellow Impact - Yellow Risk - Yellow

	Background documents The Medium Term Financial Strategy – Council 22 February 2022
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	Relevant web links
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