

Title of meeting: Cabinet

Date of meeting: 22 March 2022

Subject: Renegotiated sports and leisure facilities management contract

Report by: Director of Culture Leisure and Regulatory Services

Wards affected: All

Key decision: Yes/No

Full Council decision: Yes/No

1. Purpose of report

- 1.1. To provide the Cabinet with a summary of the contractual negotiations with BH Live, which have now concluded; and to seek Cabinet's approval to vary the existing sports and leisure facilities management contract with BH Live, on the basis that this is a key decision.

2. Recommendation

- 2.1. That the Cabinet authorises the Director for Culture Leisure and Regulatory Services to agree a contract variation to the existing sports and leisure facilities management contract, and for the Council's legal services to execute the variation as a deed.

3. Background

3.1. Introduction

- 3.1.1. On 23 March 2020, in response to the Covid-19 pandemic, the government directed all sports and leisure facilities in England to close for the foreseeable future. As a result BH Live, the operator of the council's sports and leisure facilities, saw an immediate cessation of all their income streams. The majority of BH Live staff were furloughed (and received support for 80% of their pay from central government) but BH Live were left with residual fixed costs that they had no sustainable way to meet.
- 3.1.2. Also in March 2020 the Cabinet Office published procurement policy note (PPN) 02/20 which instructed public sector contracting authorities to act to ensure suppliers at risk were in a position to resume normal contract delivery once the outbreak was over. In view of this, BH Live requested that the council waive its entitlement to collect the management fee for the sports and leisure contract and provide financial support to meet ongoing non-ameliorable fixed costs (non-



furloughed staff, buildings maintenance, residual utility costs and head office contributions).

- 3.1.3. At the same time, the Pyramids contract was based on the council covering any operational deficit and, although BH Live furloughed staff and reduced other operating costs to a minimum, the cost to the Council for the 2020/21 financial year was significant as set out in appendix A.
- 3.1.4. At the beginning of the 2021/22 financial year as the facilities were still unable to open or operate consistently due to the range of changing Covid 19 restrictions, the council agreed to BH Live's request to continue to waive the management fee and underwrite any operational deficit for the sports and leisure contract as well as continuing to underwrite the operational deficit for the Pyramids. This created a significant budget pressure for the Council which has been partly offset by a one-off grant from Sport England under the National Leisure Recovery Fund scheme and in terms of the lost income, in the region of 70% of support from central government from the Covid income support scheme up to June 2021.
- 3.1.5. Due to the imposition of further facility closures, future uncertainty and social distancing measures in early 2021 the council and BH Live agreed to extend the effect of the contract variation up to end of March 2022. These measures were approved by the council's procurement gateway board in April 2021.
- 3.1.6. During the 2021/22 financial year the operational deficit has reduced however no management fee has been received by the Council.
- 3.1.7. With the re-opening of sports and leisure facilities, the gradual return of participants, and the retreating risk of a re-imposition of closures, officers have been in dialogue with BH Live since August 2021 to negotiate post-Covid-19 contractual and financial positions.
- 3.1.8. The key issues to resolve were:
 - The level of the management fee pre-Covid-19 was never sustainable for BH Live, and they are no longer in a position to subsidise their Portsmouth operations from other contracts they hold elsewhere (ie Bournemouth).
 - The income from the management fee forms part of the Culture, Leisure and Regulatory Services budget, and so any reduction will (continue to) create a financial pressure on the service and the council in general.
 - The contract at the Pyramids has expired and is operating under a letter of intent only.
 - The council made a significant investment to transform the Pyramids pool into Exploria – an indoor adventure play and bounce attraction – and convert the Plaza conference and events space into a large multi-zone health and fitness centre.
 - Despite this, there is little prospect in the current market (which is only gradually recovering from the pandemic) of a successful procurement, at this time, of a new operator at the Pyramids as a stand-alone facility.
 - There is no lease in place for the Pyramids (albeit there is a letter of intent governing the parties' relationship) and building maintenance responsibilities are not aligned with the rest of the sports and leisure estate.

3.2. Sports and leisure facilities management contract (background)

- 3.2.1. BH Live has operated the main sports and leisure contract in Portsmouth since February 2017. When it was awarded, the contract delivered a considerable saving to the council compared with the previous operator and included PCC capital investment in the facilities of around £1.2m.
- 3.2.2. Facilities included under this contract are:
- Mountbatten Centre
 - Portsmouth Gymnastics Centre
 - Portsmouth Tennis Centre
 - Eastney Swimming Pool
 - Wimbledon Park Sports Centre
 - Charter Community Sports Centre
- 3.2.3. On appointment, BH Live reviewed the pricing model following competitor benchmarking and reduced the monthly gym membership fee by around £10 per month from the start of the contract. Between 2017 and 2020 (when the pandemic closed all sports and leisure facilities) this new pricing model drove up gym membership from 2700 in February 2017 to 5200 in February 2020 (a 90% increase). Participation was also up across all 'dry' activities – but not swimming which declined in line with national figures.
- 3.2.4. The contract was re-negotiated in 2018, due to issues with affordability and the fact that the plan to expand the gym at Wimbledon Park Sports Centre could not go ahead (primarily due to issues with car parking). This significantly reduced the revenue contribution to PCC over the period of the contract. Even with this reduction, the financial return was still more positive than it had been with the previous operator (as set out in appendix A).
- 3.2.5. BH Live's Board of Trustees and chief executive remain supportive of the long-term partnership with the council, however concerns were raised even before the pandemic that the contract was operating at a significant ongoing loss against the tendered sum.
- 3.2.6. The main sports and leisure management contract runs until the end of January 2027 and has provision to be extended by up to a further 10 years.
- 3.2.7. In response to the Covid-19 pandemic and to ensure that facilities could reopen when allowed, the council and BH Live agreed an initial contract variation which implemented the agreement outlined above whereby the council waives its entitlement to the management fee and provides financial support to meet ongoing non-ameliorable fixed costs. These measures were approved by the council's procurement gateway board in April 2021.
- 3.2.8. As part of this agreement, council officers are actively working with BH Live to scrutinise ongoing costs and levels of income under the existing open book arrangement to ensure that any ongoing deficits are kept to a minimum.

3.3. Pyramids management contract (background)

- 3.3.1. BH Live has operated the Pyramids contract since October 2013 with no operational subsidy underwrite by the Council. The contract was initially awarded

for a 5-year term. Two incidents of flooding occurred in 2014 and 2015 which meant the facility was closed for a period of time. Following the resolution of these incidents, the contract was extended by a year to 30 September 2019 when it expired.

- 3.3.2. At this point the operational losses of the Pyramids were revealed by BH Live. They amounted to £1.8m in losses over the course of the 6-year contract. This situation was clearly unsustainable and so the council entered into an open book arrangement under which it was agreed to underwrite the deficit in order to keep the facility open with the intent of taking a short period of time to understand the various scenarios available to minimise operational losses at the site.
- 3.3.3. With the contract having expired, the council and BH Live implemented an agreement, via a letter of intent from October 2019, to continue under the terms of the original contract and for the council to underwrite any operational losses. With the arrival of the Covid-19 pandemic, this arrangement was continued until the end of January 2021. Due to the imposition of further social distancing measures in early 2021, the council and BH Live agreed to extend the arrangement via a further letter of intent up to the end of March 2022 to be co-terminus with the interim arrangements for the main leisure management contract. These measures were approved by the council's procurement gateway board in April 2021.
- 3.3.4. In August 2020, following a period where resources were directed at responding to the pandemic, officers were able to resume work on addressing the situation at the Pyramids. There was already a capital allocation for renovation of the building – the bulk of the cost would be replacement or major refurbishment of mechanical plant and electrical installations and works needed to the fabric of the building such as relaying flooring extensively and redecorating most areas. An options appraisal in 2018 had concluded that the best way to minimise operational losses was instead to close the pool as it was the single most expensive element of the facilities at the Pyramids.
- 3.3.5. In February 2020, BH Live presented the council with a proposal which would transform the pool area into a ('dry') indoor adventure centre with play and trampoline elements; the Plaza events space would be transformed into a large multi-zone gym. The existing gym would be converted into group exercise studios and the Glasshouse and Solent View events spaces would be retained. This work is complete with the adventure centre having opened in August 2021 as 'Exploria' with encouraging trading results and the gym having opened in January 2022 under the existing 'BH Live Active' brand.

3.4. Negotiations

- 3.4.1. Meetings took place between council officers and BH Live representatives between August and November 2021 to arrive at a position where the objectives (as set out below) could be met while acknowledging the current uncertainties in the leisure market.
- 3.4.2. **Objectives:**
- Agree a new management fee payable to the council which reflects the fact that previous payments were unsustainable for BH Live even pre-Covid-19, but that any deleterious impact on the council's culture and

leisure budgets must be minimised. A new realistic leisure operating base trading account (LOBTA) must be agreed – one which would operate sustainably for the duration of the contract and not result in a return to negotiations as occurred in 2018.

- Revert contractually, (aside from the revised LOBTA, and some variations which have been agreed to improve performance) to the main sports and leisure management contract as awarded in 2017, ie the interim variations covering the past 2 years which waived the management fee shall expire.
- Resolve the contractual arrangements with the Pyramids. Continuing arrangements, under a letter of intent, is not acceptable to the council going forward. However, a new procurement exercise, for an operator of the Pyramids as a standalone facility is not currently desirable to the council owing to the leisure market which is only gradually recovering from the pandemic.
- Resolve the issue that the Pyramids has been occupied and operated by BH Live since 2013, but no lease had been agreed. The issue related to maintenance responsibilities, but the investment into Exploria and the new gym has largely addressed any significant maintenance risk for the operator and should allow a lease to be entered into and maintenance responsibilities at the Pyramids to be largely aligned with those of the main sports and leisure management contract.

3.4.3. Outcomes:

- **Contractual resolution for the Pyramids**

The interim contractual arrangements (letter of intent) at the Pyramids will expire on 31 March 2022 and the facility will be included in the main sports and leisure management contract via a contract variation. When the main contract was procured the OJEU contract notice explicitly included provision to accommodate additional facilities and so this represents the most appropriate route to re-enter formal contractual arrangements for the Pyramids in a way that is compliant with procurement regulations.

As the council has invested significantly in the transformation of the Pyramids into Exploria and the large well-equipped gym this arrangement for the Pyramids is initially for 2 years only with the provision to extend arrangements thereafter by agreement up to the expiry of the main contract. The agreement is that the council and BH Live will undertake a financial review after 12 months of the facility being fully open (ie in January 2023) and re-negotiate the operating surplus share arrangements including a guaranteed management fee to the council to begin in April 2023 - in light of a full 12 months trading information. This assumes that it will be agreed that the arrangements are to be extended beyond the initial 2-year period; if not, this gives the council time to procure an alternative operator.

- **Agreement on the management fee**

It was agreed that due to the capital investment made into the facility by the Council that from 1 April 2022 the Council would no longer be liable to underwrite any operating deficit from the facility and any operational surplus would be shared 75/25 preferentially to the council.

- **Resolution of the lease for the Pyramids**

The Pyramids lease from 2013 was not signed due to disagreement over maintenance responsibilities. Since then a working arrangement has been in place which, while based on the split of maintenance responsibilities from the main sports and leisure management contract, departed from it in that it contained a cap on the operator's liability for any maintenance element. This has not always worked satisfactorily.

With the large-scale changes that have been made to the Pyramids building, including the fact that a considerable amount has been spent on addressing maintenance issues, and the fact that many items which require expensive maintenance have been taken out of commission, the maintenance risk from the building is much lower than before the re-purposing project.

Consequently, it has been agreed that the maintenance responsibilities at the Pyramids will be the same as the rest of the facilities covered by the sports and leisure maintenance contract with the following exclusions:

- External glazing – repair and replacement to be the council's responsibility.
- Sprinkler system – repair and replacement to be the council's responsibility (NB the sprinkler system has been drained, capped off, and decommissioned so this provision will only apply in the unlikely event that it is required to be re-commissioned).
- The Plaza access lift – repair and replacement to be the council's responsibility (NB the plaza access lift has been decommissioned so this provision will only apply in the unlikely event that it is required to be re-commissioned).

4. Reasons for recommendations

- 4.1. The agreement reached represents the conclusion of a negotiation that has been entered into with the intent of maintaining a partnership relationship, keeping facilities open, providing an important community service, and a desire to retain a balance of risk and reward between the parties. It also acknowledges the extent of investment into facilities by the council and provides a mechanism to incentivise BH Live to drive up operating surplus.
- 4.2. This brings to a close a two-year period during which the council has incurred extensive unprecedented costs (partly offset by Government and Sport England grants) in order to retain the leisure service in a position where it can re-open following the pandemic. There are encouraging signs that participation levels are returning to pre-Covid-19 levels. This rightly returns BH Live to a position where it

is exposed to the risks and vagaries of the market, without the council underwriting operational losses.

4.3. This represents a second re-negotiation of the contract LOBTA since 2017, and both parties were motivated to reach an agreement where no further re-negotiations are required for the duration of the contract. To this end it represents a realistic position given the forecasts for the remaining six years, but one which does not return to the unsustainable pre-Covid-19 levels of management fee for the council.

4.4. The variation agreement, if approved, will come into effect on 1 April 2022.

5. Integrated impact assessment

5.1. An integrated impact assessment has been completed.

6. Legal implications

6.1. This is a proposed variation to the Council's leisure operating contract with BH Live (company registered number 07092112). The contract was publicly procured as a light touch services contract pursuant to the Public Contracts Regulations 2015 ("PCRs") under OJEU number 2016/S 068-118047 dated 7 April 2016.

6.2. Regulation 72 of the PCRs contains provisions regulating variations to concluded contracts. This includes where the original procurement provided clear variation provisions and non-substantial variations.

6.3. The original OJEU notice stated:

"The Council reserves the right to extend the scope of the contract to cover additional sporting, leisure and cultural sites and services across the City, either in whole or in part. Take up of options to extend the scope will be at the Council's sole discretion. Should these options be taken in full the per annum value could increase to approx. 13 500 000 GBP."

6.4. General principles of transparency, equal treatment and non-discrimination should be complied with. The Council must also consider and satisfy its statutory duty of best value (section 3 of the Local Government Act 1999).

6.5. The contract was originally executed by the Council under seal. The Council's Contract Procedure Rules govern that where a contract is executed under seal it may only be varied by a deed.

7. Director of Finance's comments

The financial implications of the Covid 19 impact and the contract renegotiations are included in appendix A.

To date the Council has funded any additional costs and lost income from Covid related grant funding and specific reserves. The proposals presented in this report seek to regularise the contractual position and management fee arrangements on an ongoing basis. This will present an additional net cost to the Portfolio Budget, arising from the reduction in the renegotiated management fees. The Budget approved by Full Council on 15 February 2022 has made full budgetary provision consistent with these proposed changes.

Going forward from 1 April 2022 no operational deficits are forecast however if they were to arise the Council will not be expected to provide any further support. In addition to this there is a guaranteed management fee due from the main Sports and Leisure facilities and one expected from the Pyramids from April 2023. In both cases any operational surpluses over and above the re-negotiated management fees payable to the Council will also become due to the Council on a preferential share.

Whilst there has been a requirement to increase the Portfolio's Budget to reflect all of these changes, the overall financial position still remains more favourable compared with the previous contract.

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Signed by:

Appendices:

Background list of documents: Section 100D of the Local Government Act 1972

The following documents disclose facts or matters, which have been relied upon to a material extent by the author in preparing this report:

Title of document	Location

The recommendation(s) set out above were approved/ approved as amended/ deferred/ rejected by on

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Signed by: