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**REPORT TO THE MEETING OF THE EXECUTIVE 2 DECEMBER 2020**

**PORTFOLIO: COMMUNITY**

**REPORT FROM ASSISTANT DIRECTOR, ASSETS & COMMERCIAL**

**SUBJECT: LEISURE SERVICE PROVISION FROM APRIL 2021**

**1 DECISION BEING RECOMMENDED**

- 1.1 That, following consultation with the Portfolio Holder for Community and the Portfolio Holder for Finance, the preferred option set out in paragraph 6 of this report for leisure service provision from 1 April 2021 be approved.
- 1.2 That additional budget of £123,732 over the lifetime of the contract extension be approved to enable the preferred option to be implemented, subject to agreement by Fusion Lifestyle ("Fusion") to the proposed letter of variation to the current contract.
- 1.3 To agree to fund the additional costs via a Leisure Contract Smoothing Reserve to be created by moving monies currently held within the Business Rates Smoothing Reserve which currently has a balance of c£1.3m.
- 1.4 That authority be delegated to the Assistant Director, Assets & Commercial in consultation with the Portfolio Holder for Community to enter into a contract variation with Fusion to implement the preferred option.

**2 REASON/S FOR RECOMMENDATION**

- 2.1 The COVID-19 pandemic has created a significant economic impact within the leisure sector in the UK, both public and private. It is projected to have a longer-term impact on the industry due to both the restrictions operators will have to operate under and because of reduction in demand from site users' confidence in returning to use them.
- 2.2 As agreed at the meeting of the Executive in August 2020, in consultation with the Portfolio Holder for Community and the Portfolio Holder for Finance, the Assistant Director, Assets & Commercial initiated negotiations with Fusion to agree a new commercial arrangement for the operation of the Council's leisure sites beyond the 2020/21 financial year.
- 2.3 As reported to the Executive in August 2020 it was proposed to modify the existing contract terms further to include the period from April 2022 to a new end date, which would enable the Council to be clearer about its proposed next steps for future service provision.

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### 3 SALIENT INFORMATION

- 3.1 This report sets out the contract negotiation process undertaken, the commercial considerations that are required as a result of the impact of COVID-19 on the leisure industry nationally and presents costed options for the Council's future leisure service provision.
- 3.2 The Council's existing leisure contract with Fusion expires on 31 March 2022.
- 3.3 Fusion manages the following facilities as part of that contract:
- Clements Hall Leisure Centre;
  - Rayleigh Leisure Centre;
  - The Mill Arts & Events Centre;
  - Freight House (currently closed); and
  - Castle Hall.
- 3.4 The Council had planned to tender for a new leisure contract to commence on 1 April 2022, in accordance with its Leisure & Cultural Services Strategy. Officers had been working with the Sport, Leisure and Culture Consultancy ("SLC") to prepare a procurement exercise which was due to commence in January 2021. This was considered the latest date a procurement exercise could begin in order to run a competitive procedure prior to the current contract ending.
- 3.5 COVID-19 forced the Council to reconsider its approach, since procuring a new contract in a commercially uncertain environment would be unlikely to achieve value for money or incentivise innovation or investment by a service provider.
- 3.6 Following the report to the Executive in August 2020 the Council and Fusion agreed and signed a letter of variation to the leisure contract to enable the reopening of four of the five leisure sites on a sustainable basis for both parties on an open book approach from 1 August 2020 to 31 March 2021.
- 3.7 The letter of variation provides that if, on or before 18 December 2020, or such later date as the parties agree, it has not been possible to agree revised arrangements then the Council may terminate the contract for convenience by giving not less than 4 months' written notice to the contract ("Non Default Termination Notice"). The implications of terminating the contract are outlined in paragraph 7.

### 4 REOPENING OF LEISURE SITES

- 4.1 Clements Hall Leisure Centre and Rayleigh Leisure Centre reopened in a COVID-19 secure phased approach on 20 August 2020.

The Mill Arts & Events Centre and Castle Hall reopened in a COVID-19 secure phased approach on 30 October 2020.

Freight House remains closed as per the recommendation of the Executive in August 2020.

- 4.2 Fusion's approach to the reopening of the facilities was shaped by the advice from Central Government, National Governing Bodies of Sport and Trade Associations, such as UKActive and Swim England. Their objective was to ensure that they could create a COVID-19 secure facility for customers and staff that would give them the confidence to return to the centres.
- 4.3 All sites had to close again from 5 November 2020 further to Central Government's national restrictions for a 4-week period to 2 December 2020.
- 4.4 Participation and financial performance at Clements Hall Leisure Centre and Rayleigh Leisure Centre has been in line with Fusion's forecast up to and including the end of September 2020.
- 4.5 Customer feedback since the August reopening from both leisure centres has been broadly positive. The Council receives a weekly log of customer comments, complaints and compliments from Fusion. Numerous positive comments have been received regarding the measures undertaken by Fusion to ensure the sites are COVID-19 secure and how safe site users have felt using them. However, frustration has also been raised regarding when certain sports would restart, timetabling and opening hours. Fusion has reiterated throughout that they are following Government and National Governing Body guidance and that all operational matters are under constant review. The poor communication during the first lockdown has also been fed back to Fusion senior managers and their Chief Executive.
- 4.6 Very little feedback has been received regarding the decision not to reopen Freight House or the decision not to reopen The Mill Arts & Events Centre and Castle Hall until late October. Officers have supported customers who were due refunds from Fusion from bookings at Freight House and The Mill Arts & Events Centre, where there had been long delays in these being processed and poor communication on the part of Fusion.
- 4.7 Officers continue to be in regular contact with Braintree District Council and Southend Borough Council who also have leisure operating contracts with Fusion and also Local Authorities nationally, where Fusion is their leisure operator. The Council's Acting Managing Director has participated in a meeting with those authorities and the Chief Executive of Fusion where assurances were provided about the ongoing resilience of the proposed commercial model and deliverability of services in the future.

## **5 Contract Extension Negotiations and Outcomes**

- 5.1 Since procuring a new contract in a commercially uncertain environment is unlikely to achieve value for money or incentivise innovation or investment by an operator officers, assisted by SLC, have concluded that remaining with Fusion by extending the current contract is the only commercially viable

mechanism to secure ongoing leisure provision post 31 March 2021 when the letter of variation expires. (The current contract ends on 31 March 2022 but any new arrangement would apply from 1 April 2021.) A period of 2 or 3 years is the minimum that Fusion would consider to provide them with the necessary certainty and is a period sufficient to enable the wider market to recover, enabling the Council to review its options at that point.

- 5.2 Throughout September and October officers have held regular dialogue meetings with Fusion to negotiate terms for a possible contract extension. The Council has received external expert advice from SLC throughout this dialogue phase and they have reviewed and scrutinised all income and expenditure projections. SLC has completed a number of leisure operating contract procurement projects for local authorities. They were also appointed by Sport England as the lead author of the new Leisure Services Delivery Guidance and to develop the recently published Strategic Outcomes Planning Guidance.
- 5.3 A report from SLC of the process followed and outcome can be found in Appendix 1. An Exempt version including further commercially sensitive information can be found in Appendix 2

They concluded that, given the uncertainty regarding the current and future leisure market, potential ongoing restrictions and lack of clarity on medium and longer term implications of COVID-19, the cost for the service is considered to be reasonable.

- 5.4 The net annual costs of operating a 3-year contract extension with the Mill Arts & Events Centre, Castle Hall and Freight House mothballed as per Fusion's submission are shown in Table 11.

**Table 1: 3-Year Contract Extension Total - Mill Arts & Events Centre, Castle Hall and Freight House mothballed**

2021/22	2022/23	2023/24	2024/25	Total
-£239,483	-£182,215	-£84,369	-£2,384	-£508,451

- 5.5 This shows a total cost of £508,000 over a 4-year period – an average cost of £127,000 p.a. before taking into account leisure service related project and salary costs which average £108,000 p.a. The total average cost of delivering leisure services of £235,000 p.a. compares to the current annual budget of £165,000, creating an average pressure of £70,000 p.a. However, the existing Freight House and Mill Arts & Events Centre sites are due to be redeveloped as part of the Council's Asset Delivery Programme in September 2021 and June 2023 respectively. This will reduce the average total budget pressure over 4 years to c.£124,000 (or an average of £31,000 p.a.) as Fusion will no longer have to maintain/run these sites for that period. Were the Asset Delivery

Programme timescales to be delayed this would increase the overall budget pressure.

- 5.6 Two different variations of the contract have been modelled over each 2 or 3 year extension period: Option 1 which assumed the Mill Arts & Events Centre and Castle Hall sites reopen until the redevelopment of the Mill Arts & Events Centre site in June 2023 and Option 2 which assumed the Mill Arts & Events Centre and Castle Hall sites are mothballed. Both options assume that the Freight House site remains mothballed, as agreed by the Executive in August 2020. Both options assume Clements Hall and Rayleigh Leisure Centres remain open.

**Table 2: Contract Variations**

<b>Fusion subsidy plus project and salary costs for Option 1:</b>					
Freight House mothballed to end Sep 21 then disposal, Mill & Castle Hall open until disposal end June 2023, other sites open	<b>2021/22</b>	<b>2022/23</b>	<b>2023/24</b>	<b>2024/25</b>	<b>TOTAL</b>
	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>
2 year extension	£558,953	£395,493	£301,029		<b>£1,255,476</b>
<i>MTFS pressure compared to current budget</i>	<i>£393,953</i>	<i>£230,493</i>	<i>£136,029</i>		<i><b>£760,476</b></i>
3 year extension	£426,034	£335,766	£154,460	£44,443	<b>£960,703</b>
<i>MTFS pressure compared to current budget</i>	<i>£261,034</i>	<i>£170,766</i>	<i>£10,540</i>	<i>£120,557</i>	<i><b>£300,703</b></i>

<b>Fusion subsidy plus project and salary costs for Option 2:</b>					
Freight House mothballed to end Sep 21 then disposal, Mill & Castle Hall mothballed to end June 2023 then disposal, other sites open	<b>2021/22</b>	<b>2022/23</b>	<b>2023/24</b>	<b>2024/25</b>	<b>TOTAL</b>
	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>
2 year extension	£467,121	£328,269	£277,315		<b>£1,072,705</b>
<i>MTFS pressure compared to current budget</i>	<i>£302,121</i>	<i>£163,269</i>	<i>£112,315</i>	<i>£165,000</i>	<i><b>£412,705</b></i>
3 year extension	£334,202	£268,542	£136,545	£44,443	<b>£783,732</b>
<i>MTFS pressure compared to current budget</i>	<i>£169,202</i>	<i>£103,542</i>	<i>£28,455</i>	<i>£120,557</i>	<i><b>£123,732</b></i>

- 5.7 Fusion has based their projections on both UK Active guidance and their knowledge and operating experience. This is a reasonable approach given the current uncertainty created by the pandemic. They don't believe that they will start to move towards more normal operating regimes and revenue generation until the latter part of 2021.
- 5.8 Fusion has mitigated against reduced revenue income by implementing cost savings across the business. They have renegotiated their key supply contracts and adjusted these as far as possible to the new revenue levels.
- 5.9 Fusion has confirmed they have successfully secured a loan through the Coronavirus Large Business Interruption Loan Scheme (CLBILS). The purpose of this loan is to fund their ongoing working capital requirements and investment costs in light of the impact of COVID-19.

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**6 PREFERRED OPTION**

- 6.1 In consultation with the Portfolio Holder for Community and the Portfolio Holder for Finance the financial projections provided by Fusion have been reviewed, challenged, and carefully considered. The Council values its leisure facilities and the important role they play in the health and wellbeing of residents although this needs to be balanced and considered with the impact that COVID-19 has had on the industry nationally and the local impact on the increased costs to manage the facilities.
- 6.2 The preferred option is that the current leisure contract with Fusion is extended for a period of 3 years beyond the existing term taking it to 31 March 2025 with the following changes to the sites within the portfolio:
- 6.3 Freight House will remain closed as per the recommendation in the report to August's Executive since this is one of the buildings proposed for early redevelopment as a new Community and Civic Space within the Council's Asset Delivery Programme.
- 6.4 The Mill Arts & Events Centre and Castle Hall will not reopen following the national enforced closure between 5 November and 2 December. This decision is justified because there has been an evidenced lack of demand for the facilities during the pandemic as users have not been able to operate within COVID-19 restrictions and customer confidence in returning to the sites has been low. The Council is satisfied that Fusion was proactive in looking to secure bookings in the lead up to reopening but before the pandemic the sites ran at a significant loss and therefore the cost to operate the sites in the current climate is unsustainable. In addition, the Mill Arts & Events Centre also forms part of the Asset Delivery Programme, where the proposal is to redevelop this site for residential use with flexible space, including space retained for Council and community uses. The Council will explore the options for alternative commercial or community use of Castle Hall.
- 6.5 Council officers from the Leisure & Cultural Services team will continue to work with and support groups or organisations that are currently, or were previously, using the Freight House, the Mill Arts & Events Centre or Castle Hall and who would like assistance to identify alternative local facilities where possible.
- 6.6 The total additional cost to the Council of this option over the course of the 3-year extension to the current contract (4-year agreement to 2024/25) is estimated to be £123,732, based on the annual profile set out below.

**Table 3: Anticipated Net Additional Cost of the Preferred Option in 2021/22**

<b>Fusion subsidy plus project and salary costs for Option 2:</b>					
Freight House mothballed to end Sep 21 then disposal, Mill & Castle Hall mothballed to end June 2023 then disposal, other sites open	<b>2021/22</b>	<b>2022/23</b>	<b>2023/24</b>	<b>2024/25</b>	<b>TOTAL</b>
	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>	<b>£</b>
3 year extension	£334,202	£268,542	£136,545	£44,443	<b>£783,732</b>
<i>MTFS pressure compared to current budget</i>	<i>£169,202</i>	<i>£103,542</i>	<i>-£28,455</i>	<i>-£120,557</i>	<b><i>£123,732</i></b>

- 6.7 The actual amounts paid in Year 1 (2021/22) will be based on the month by month financial performance of Fusion Lifestyle over the period, so will vary, but will be subject to a total cap assumed within the 2021/22 figure above. In years 2 to 4 of the new agreement the Council would pay a fixed unitary charge to Fusion.
- 6.8 The total additional cost is shown net of budgeted payments already assumed in the Council's MTFS and inclusive of salaries for two Council employees totalling c£90,000 and an annual events project budget of £14,500. The Council will also continue to meet the business rates obligations for the leisure sites, this is no change to the current arrangement with Fusion.
- 6.9 Fusion's actual financial performance in Year 1 would be reviewed monthly by officers on a fully open book basis. This will require Fusion's management accounts to be submitted setting out a detailed breakdown of actual costs incurred, and income generated, for each site. These would be compared to the baseline projections above, and any variations interrogated to ensure they can be reasonably explained by Fusion.
- 6.10 As with the current open book agreement Fusion will be incentivised to outperform their income and expenditure forecasts by retaining the initial 20% of any improvement in their figures but will also be liable for the first 20% of any underperformance. The total amount for Year 1 payable to Fusion will also be capped, as set out in paragraph 6.7.

## **7 ALTERNATIVE OPTIONS CONSIDERED**

- 7.1 The Council has the option to keep open none/some/all of its leisure facilities. The estimated cost of operating each site for both a 2 year and 3-year extension period is set out in Table 2 above.
- 7.2 There are also different models for leisure service delivery. Table 4 formed part of a report to the Executive in September 2019 regarding the potential leisure facility provision options and the advantages and disadvantages of each. The In House Management and LATCo options were not recommended at the time and the advantages and disadvantages remain the same now as they were then.

TABLE 4

Delivery Option	Advantages	Disadvantages
In House Management	<p>The Council has complete strategic and day to day control of services.</p> <p>Direct control of relationships with other Council services</p>	<p>The Council retains liability for the operational performance of the services.</p> <p>The Council retains liability for the capital maintenance costs associated with the facilities and any capital funding requirements.</p> <p>Limited access to the benefits of developing new opportunities and from economies of scale and also to the wider knowledge gained by other operators for innovation and development.</p> <p>The present Contractor currently employs approximately 125 staff, which would result in a significant increase to the Council's current workforce.</p>
Contract (current model)	<p>Opportunity for operator to bring economies of scale and efficiencies</p> <p>Broader expertise and experience of the operator</p> <p>The Council has greater certainty of revenue and capital costs or returns</p> <p>Council can set out its requirements through a specification</p>	<p>The Council does not have direct control over the service</p> <p>Operator may prioritise commercial rather than social objectives e.g. profit (unless stipulated in the contract)</p> <p>Potential loss of community focus (unless stipulated in the contract)</p>



New organisation (LATCo)	<p>The Council retains ownership of the Company</p> <p>Group Structure already established</p> <p>Operational risks can be transferred to the new company</p> <p>The Council are represented on the Board of the Company by Council Officers to ensure Council's strategic outcomes are delivered</p>	<p>Limited expansion of the business to create economies of scale</p> <p>The Council does not have direct control of the day to day operation of the business</p> <p>Insufficient expertise and resource of Council Officers</p> <p>The current Contractor currently employs approximately 125 staff, which would result in a significant increase to the Council's current workforce</p>
Asset Transfer	<p>The Council receives a capital receipt (long lease)</p> <p>The Council transfers all the risks of operating the facilities to the new owners</p>	<p>The Council has no leisure facilities under its control from which to provide public leisure services</p> <p>New owners may seek to remove any leisure facilities and services in the future and replace with more commercial focus (unless built into the agreement)</p> <p>Likely to be unpopular with users on lower incomes as new facilities may incur a premium price</p>

- 7.3 It is considered unviable for the Council to operate leisure services directly itself in the short-medium term, due to a lack of available resource/expertise within the Council. In the event of a contract extension not being agreed with Fusion, this would result in no leisure facilities being available for residents until the Council was able to secure another service provider. The Council would also incur significant costs to mothball the sites during this period. This range is

influenced by whether the sites were mothballed with a view to reopening or a hard closure. A fully competitive tendering process for a new leisure contract would take 12-15 months to run.

- 7.4 In April 2019 officers carried out a Soft Market Testing exercise as part of the work towards a new leisure contract from April 2022. As part of the research and investigation for this report officers have again spoken to each of the operators that took part in that process.
- 7.5 Timescales did not allow them the time to provide a financial projection by way of comparison, therefore there would be an unquantifiable financial risk with this option.
- 7.6 Operators confirmed that they would be able to take over the operation of the Council's leisure sites. However, the incumbent operator has certain advantages that would impact any financial agreement in their favour, including the cost of any mobilisation. Capital investment is also required in the sites and Fusion also have the knowledge of the local market. As highlighted in exempt appendix 2, operators are adopting a more risk averse position.

## **8 RISK IMPLICATIONS**

- 8.1 The financial risks are set out in section 9 of this report.
- 8.2 The legal risks are set out in section 10 of this report.
- 8.3 The Leisure & Cultural Services Team will continue to work in partnership with Fusion; closely monitoring the contract and remaining in regular contact with Centre Managers and Business Manager.

## **9 RESOURCE IMPLICATIONS**

- 9.1 See paragraphs 6.6 to 6.10 which set out the additional cost of the preferred option.
- 9.2 The Council would seek to fund the additional costs of the preferred option via a Leisure Contract Smoothing Reserve to be created by moving monies currently held within the Business Rates Smoothing Reserve which currently has a balance of c£1.3m. The additional costs in 2021/22 and 2022/23 (above the current annual budget of £165,000) will be drawn from this reserve. The annual leisure contract budget will then be reduced in 2023/24 and 2024/25 in line with expected profile of costs, as set out in Table 3 at paragraph 6.6.
- 9.3 Monitoring and oversight of the new contract will be carried out in-house using existing resources.
- 9.4 On 22 October 2020 to address the ongoing challenges local authority leisure centres are facing, the Department for Digital, Culture, Media and Sport confirmed that £100 million will be used to introduce a new fund which will support council leisure centres most in need. Further details on the scheme will

be set out shortly, which officers will proactively monitor with a view to accessing the funding and mitigating against costs.

## **10 LEGAL IMPLICATIONS**

- 10.1 Regulation 72 of the Public Contracts Regulations 2015 allows for contracts to be modified without the need of having to go through the process of retendering.
- 10.2 Regulation 72(1)(b) covers circumstances where additional works, services or supplies by the original contractor have become necessary and were not included in the initial procurement, where a change of contractor:
- a) cannot be made for economic or technical reasons such as requirements of interchangeability or interoperability with existing equipment, services or installations procured under the initial procurement, or
  - b) would cause significant inconvenience or substantial duplication of costs for the contracting authority, provided that any increase in price does not exceed 50% of the value of the original contract.
- 10.3 Regulation 51 sets out the procedure which the Council is required to follow which in essence is a publication of a notice with prescribed information contained in law.
- 10.4 The procurement position would need to be reviewed again if negotiations were to slip into 2022, as there may be changes to the regime following Brexit.
- 10.5 Exempt appendix 3 sets out the process by which the contract can be extended.
- 10.6 The current contract does not automatically entitle Fusion to any additional payments, support or relief where a pandemic or other event occurs which is outside its control. If there are further extended periods where there are significant restrictions on the use or availability of the sites, then Fusion might seek to argue that as it is no longer possible for the contract to be performed for a significant period the contract has been frustrated and to claim that the law gives them the right to terminate the contract and walk away.

## **11 EQUALITY AND DIVERSITY IMPLICATIONS**

- 11.1 The Public Sector Equality Duty applies to the Council when it makes decisions. The duty requires us to have regard to the need to:
- To eliminate unlawful discrimination, harassment and victimisation
  - To advance equality of opportunity between people who share a protected characteristic and those who do not

- To foster good relations between those who share a protected characteristic and those who do not
- 11.2 The protected characteristics are age, disability, gender, race, sexual orientation, religion, gender reassignment, marriage/civil partnerships, pregnancy/maternity.
- 11.3 The Equality Impact Assessment (EIA) indicates that the proposals in this report will have a disproportionately adverse impact on any people with a particular characteristic.

Loss of community resource.

As the Mill Arts & Events Centre and Castle Hall will not reopen users of the sites will be unable to hold their meetings, events or functions there and will need to find an alternative venue.

This impact will be mitigated against as outlined in section 3.4 of the EIA.

I confirm that the above recommendation does not depart from Council policy and that appropriate consideration has been given to any budgetary and legal implications.



LT Lead Officer Signature: \_\_\_\_\_

**Assistant Director, Assets & Commercial**

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If you would like this report in large print, Braille or another language please contact 01702 318111.



# Briefing Note – Leisure Contract Extension

Rochford District Council

November 2020

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## **1.1 Introduction**

- 1.1.1 SLC was appointed by Rochford District Council in March 2020 to support the Council with the re-procurement of their Leisure Operating Contract. The current contract with Fusion Lifestyle (FL) is due to end on 31 March 2022. As a result of the Covid-19 pandemic, the Council's facilities were forced to close between March and August, and a formal variation of the existing contract with FL was required.
- 1.1.2 A variation to the contract with additional capped funding was agreed by the Council and FL in August 2020 for the operation of the facilities (and mothballing of Freight House) until the end of the current financial year.
- 1.1.3 The letter of variation also acknowledged that, given the impact of Covid-19 on the leisure sector, the terms of the existing contract are unlikely to be capable of being met for the remainder of the contract term. The negative impact on the wider market and the ability of operators to respond positively to a procurement opportunity in Rochford was also considered, and, as a result, the letter of variation undertook to seek to negotiate and agree with FL an extension to the current contract term.
- 1.1.4 The re-procurement of the Contract was therefore postponed and SLC was engaged to support the Council in seeking to agree a new commercial arrangement with FL for the operation of the facilities beyond the current financial year.

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## **1.2 Submission Requirements**

- 1.2.1 A document was developed in consultation with the Council which set out the Council's submission requirements from FL. The proposal from FL was to include the period from 1 April 2021 to 31 March 2022 and a potential extension to the original contract period of either 2 or 3 further years.
- 1.2.2 The submission requirements document set out the Council's key Strategic Objectives for the services, the facilities and services within scope (including options to include or exclude Freight House and / or the Mill Arts & Events Centre and Castle Hall, and the inclusion of a new Active Communities programme designed to increase participation by under-represented groups), key areas of risk allocation and the proposed period of a new agreement.
- 1.2.3 It was agreed that FL's submission proposals should be based on 2021/22 operating on a similar basis to the current agreement, i.e. on an open book basis with a capped liability cap and 80:20 benefit and risk share between the Council and FL respectively. The remaining years of the new agreement (whether under a 2 or 3 year extension), would then be based on a fixed management fee (or unitary charge) arrangement.
- 1.2.4 The submissions were to assume the continued operation of all of the facilities within scope throughout the period, with variant options showing the impact of removing Freight House (mothballed), the Mill Arts & Events Centre and Castle Hall, or all of these from the scope of the contract.
- 1.2.5 The figures in this briefing note show the submissions including all facilities within scope for the duration of the period. The financial variants for the removal of the Mill, Freight House or both are also shown, based on the removal of net operating costs for the facility and a reduction in irrecoverable VAT and (in the case of the Mill) the Fusion margin.
- 1.2.6 The submission requirements were provided to Fusion Lifestyle on 23 September and an initial submission deadline set for 9 October, with a viewing to entering a period of negotiation and reaching a final submission by 30 October.



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### 1.3 Fusion Lifestyle Submissions and Negotiation

**This section is redacted for reasons of commercial sensitivity.**

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### 1.4 Conclusions

- 1.4.1 The Council has been placed in a very challenging position due to the impact of Covid-19 upon its leisure service and the timing of this pandemic in relation to the existing contract with FL. In seeking to extend the contract with FL, it is negotiating with a single partner operator who has no certainty about the future of the market and which is itself in a challenging financial position as a result of Covid-19.
- 1.4.2 Throughout this process of negotiation, income and expenditure projections included in each of FL's submissions have been reviewed and scrutinised by SLC and the Council and a series of queries and clarifications have been discussed with FL through a series of meetings and email correspondence, leading to submission of a final proposal.
- 1.4.3 Given the uncertainty regarding the ongoing impact of Covid-19 on leisure services across the country, it is extremely difficult to project how the industry may recover and over what period. SLC are of the view that the expenditure projections, proposed level of margin and support service costs are broadly reasonable and in line with a reduction compared to FL's pre-Covid costs and with what would be expected from an operator of this scale under the circumstances.
- 1.4.4 The income projections provided by FL appear conservative, although it is difficult to predict how the market will recover in the short to medium term and there is no evidence to support the extent or speed of recovery. As FL will take on all the commercial risk on income and be committed to receive fixed unitary charge from 2022 onwards, it is understandable that they have taken a cautious view to protect their position and have little incentive to adopt a more optimistic stance.
- 1.4.5 In view of this, SLC believes it is very important that a mechanism is agreed and implemented which allows the Council to see some of the benefits of an improved income position if the actual income in later years is significantly higher than projected. An income share arrangement provides the most advantageous means of securing this from the Council's perspective and should require minimal oversight and scrutiny from Officers. It is common within the market for operators to strongly resist income share arrangements (as FL has done through this process), as they argue that any associated increased expenditure required to achieve the higher levels of income is not taken into account by this mechanism. It is therefore positive that that Council has succeeded in securing agreement with FL to accept this position.
- 1.4.6 Based on the figures provided by FL, the lowest cost option to the Council would be to continue operating Clements Hall and Rayleigh Leisure Centres under a 3-year extension and to mothball the Mill Arts & Events Centre in advance of its redevelopment as part of the Asset Delivery Programme and continue to mothball Freight House. The 3-year extensions provide a lower overall cost compared with the 2-year extensions as a result of being able to spread the building condition survey costs over a longer period and the continued growth in income projected in year 3.
- 1.4.7 The cost of a 3-year contract extension with the Mill and Freight House mothballed as per FL's 6 November submission is shown in Table 66.

**Table 6: 3-Year Contract Extension Total - Mill and FH removed**

2021/22	2022/23	2023/24	2024/25	Total
-£239,483	-£182,215	-£84,369	-£2,384	-£508,451

- 1.4.8 This shows a total cost of £508K over a 4-year period – an average cost of £127K per year.
- 1.4.9 Given the uncertainty regarding the current and future leisure market, potential ongoing restrictions and lack of clarity on the medium and longer term implications of Covid-19, this figure is considered to be a reasonable cost for the service. Although the income projections are considered to be cautious, the Council is able to benefit from any significant overperformance against these projections through the agreed income share arrangements.
- 1.4.10 The alternative to agreeing a contract extension with FL available would be to resume the process of procuring a new contract from April 2022. The timescales to do this would be challenging but achievable, but with a number of associated risks. The operator market is in an uncertain position with some operators not currently exploring new contract opportunities and all are understandably adopting a more risk averse position, seeking to share more of the major risk areas with local authorities (e.g. utilities benchmarking) and to protect themselves against similar future closure and restrictions.
- 1.4.11 It is possible that an initial period of open book would be required to provide more comfort to bidders in the first year the overall financial position would be less favourable than it would have been pre-Covid or could be in the future when operators have more certainty over the leisure market and recovery of demand for facilities and services.
- 1.4.12 This alternative would also require the negotiation of terms for the final year of the contract with FL which would need to be on a similar open book basis as the current financial year. It is also possible that, without the incentive of a contract extension, FL would insist on a margin in their costs for this final year. The Council would have very little leverage in negotiating the position for this final year and the costs would likely be higher than those included for 2021/22 within the financial submission for the contract extension.





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