



## CABINET REPORT

<b>Report Title</b>	<b>Grant of property leases and financial and management agreements to Northampton Leisure Trust (Unity Leisure)</b>
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**AGENDA STATUS:** Public

<b>Cabinet Meeting Date:</b>	14 <sup>th</sup> March 2018
<b>Key Decision:</b>	Yes
<b>Within Policy:</b>	Yes
<b>Policy Document:</b>	No
<b>Directorates:</b>	Regeneration, Enterprise & Planning, and Customers & Communities
<b>Accountable Cabinet Member:</b>	Councillor Tim Hadland
<b>Ward(s)</b>	All

### 1. Purpose

To seek agreement of Cabinet:

- 1.1 To grant new leases for a term of 30 years to Unity Leisure (trading as Northampton Leisure Trust) on three leisure centres owned by Northampton Borough Council (Lings Forum, Danes Camp, Mounts Baths), in accordance with the terms and conditions set out in this report.
- 1.2 For the Council to either lend up to £3m for a period to be agreed to Unity Leisure, or act as guarantor for a similar amount, for the purpose of improving the aforementioned three leisure centres.

## **2. Recommendations**

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That Cabinet agrees that:

- 2.1 Three new Full Repairing and Insuring leases be granted under the Landlord and Tenant Act 1954 to Unity Leisure for the three leisure centres owned by Northampton Borough Council (Lings Forum, Danes Camp, Mounts Baths), for a period of 30 years. The combined rent will be £51,000 per year plus any addition for building insurances and VAT where applicable, and will be in accordance with the terms and conditions set out in this report, which reflects a discount from market rent of £22,500 per annum.
- 2.2 The Head of Regeneration, Economic Development & Assets be authorised to complete the above leases in consultation with the Borough Secretary & Monitoring Officer and the Cabinet Member for Regeneration, Enterprise and Planning.
- 2.3 It approves in principle either the lending of up to £3m to Unity Leisure or acts as guarantor for commercial lending in a similar amount, for the purpose of carrying out capital improvement works on the aforementioned three Leisure Centres.
- 2.4 The Operating Agreement between the Council and Unity Leisure be amended to remove the Council's option to close any one or more of the leisure centres on providing not less than six months' notice.
- 2.5 The Operating Agreement between the Council and Unity Leisure be amended to remove any requirement for a management fee to be paid by the Council to Unity Leisure, this amendment to apply retrospectively back to 2014/15.
- 2.6 The Council's Capital Programme be increased by the amount of the agreed loans in any given year, to be funded entirely by repayments from Unity Leisure.
- 2.7 Authority be delegated to the Chief Finance Officer acting in consultation with the Borough Secretary & Monitoring Officer and the Cabinet Member for Finance to approve the terms of the necessary loan or guarantee agreements following completion of necessary due diligence checks, ensuring that the Council is not exposed to unacceptable financial loss or liability.
- 2.8 The Chief Finance Officer be instructed to amend the appropriate revenue budgets to reflect the agreed level of rental income and savings on repairs and maintenance and insurance.
- 2.9 Authority be delegated to the Borough Secretary & Monitoring Officer in consultation with the Chief Finance Officer and the Head of Regeneration, Economic Development & Assets the power to complete all the relevant documentation, including the loan agreements, leases and Guarantee, as relevant.

## **3. Issues and Choices**

### **3.1 Report Background**

- 3.1.1 Unity Leisure trading as Northampton Leisure Trust (NLT) was established by the Council in April 2011 to operate the three Council owned leisure centres, Lings Forum, Danes camp, Mounts Baths, and to deliver sports development, health and play services.
- 3.1.2 A fifteen year Operating Agreement (with the provision to extend the agreement for further periods up to a further fifteen years) was put in place between the Council and NLT which entailed the Council paying a fee to NLT in return for agreed outcomes. A thirty year lease for the three leisure centres was also entered into at a peppercorn rent.
- 3.1.3 The lease permitted termination by the Council upon determination of the Operating Agreement for any reason, and the Operating Agreement provided the Council with the option to close any one or more of the leisure centres on the provision of not less than six months' notice.
- 3.1.4 It is generally accepted that NLT has thrived since its inception in 2011, not only delivering its original portfolio of services but also expanding its remit and taking on new business.
- 3.1.5 The success of NLT enabled the management fee payable by the Council to NLT to be reduced year on year down to zero by 2014/15. It is proposed that the Operating Agreement between the Council and NLT be amended to reflect the position reached in 2014/15, and the intention of the parties going forward is that no management fee will be payable in the future.
- 3.1.6 For NLT to continue to grow and expand as a leisure provider, it is timely to review the arrangements that were originally put in place in relation to the Operating Agreement and the leases.
- 3.1.7 It is now proposed that three new leases are entered into, one for each of the three leisure centres.
- 3.1.8 It is further proposed, in order to enable NLT to benefit more fully from the new lease arrangements, that the Operating Agreement is extended so as to be concurrent and co-terminus with the new leases, and the Council's right to close any one or more of the leisure centres with six months' notice is removed.
- 3.1.9 The proposed new leases and the proposed changes to the Operating Agreement will give NLT much greater security of tenure enabling it to borrow and access funding more readily, thus improving the services it is able to deliver to the people of Northampton.
- 3.1.10 The proposed new leases will also transfer additional liability for repairs and maintenance of the buildings and plant from the Council to NLT.

## **3.2 Issues**

3.2.1 The development of the proposals set out in this report have required the careful balancing of the requirements of both the Council and NLT against financial, legal and other risk factors so as to find the best way forward for NLT service users and the wider population of Northampton.

## **3.3 Choices (Options)**

3.3.1 The recommendations of this report are interdependent and represent a single package that has been provisionally agreed in its entirety with NLT. Cabinet can therefore only choose to accept or decline all the recommendations.

3.3.2 If Cabinet choose to decline the recommendations of this report it may request that alternative proposals are developed, and for negotiations to be re-opened with NLT so that alternative recommendations can be brought forward to Cabinet in the future.

3.3.3 In developing the recommendations of this report, consideration was given to the duration and terms of the three leases. The options considered for the duration of each lease were a 99 year lease outside the provisions and protections of the 1954 Landlord and Tenants Act, with a rolling development break from year 15 onwards and no liability for external repairs and maintenance, or a 30 year lease granted within the terms of the 1954 Landlord and Tenant Act.

3.3.4 It was determined that the latter form of lease would give NLT the security of tenure necessary for it to secure long term development funding, and protect the long term strategic interests of the Council as owner of the properties.

3.3.5 The options considered for the terms of the lease were to make it Internal Repairing only, or a Full Repairing and Insuring lease (FRI). The FRI lease is preferred on the basis that this makes all building maintenance and repairs the responsibility of NLT, which is both beneficial to the Council, and allows NLT to better manage its own finances and operational requirements.

## **4. Implications (including financial implications)**

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### **4.1 Policy**

4.1.1 The recommendations of this report are within policy and have no policy implications.

### **4.2 Resources and Risk**

#### Leases

4.2.1 It is proposed to grant NLT a Full Repairing and Insuring lease (FRI) for a 30 year term on each property. Independent valuers were engaged to recommend appropriate market rents for the 3 properties on an FRI basis, taking into account the likely future external maintenance and repairs that may be required.

- 4.2.2 The total rent recommended for the three properties was assessed at £73,500 over a 30 year term. However, in negotiation with NLT, it was argued by NLT that a move from a peppercorn rent to circa £70,000 a year could not be sustained, and it was therefore agreed by the Council that a lower level of rent would be acceptable in order that all parties could be confident in the long term delivery of services at the current level.
- 4.2.3 A reduction of £22,500 was therefore agreed, leaving an annual rental of £51,000. This will be subject to upwards-only rent reviews every 5 years, with increases based on the Consumer Price Index (CPI).
- 4.2.4 Section 123 of the Local Government Act 1972 provides that a Council 'may dispose of land held by them in any manner they wish', and that such disposal should not be for less than the best consideration that can reasonably be obtained between willing parties. The granting of a long lease is classed as a disposal for the purposes of Sect.123, so the Council would normally be required to seek the best consideration from NLT. However, in certain circumstances this requirement can be waived.
- 4.2.5 The General Consent Order allows a Council to dispose of land for less than the best consideration where it considers that the disposal will contribute to the social, economic or environmental well-being of the area, and the total undervalue does not exceed £2,000,000. In this instance it is recommended that the 3 leases be granted to NLT at an under value of £22,500 per annum, i.e. £675,000 over the 30 year term of the leases. It is considered that this figure still represents value for money and that the requirements of Sect.123 are satisfied for the following reasons:
- The future repair and maintenance costs of the 3 buildings are potentially significant, and if we do not conclude the leases these costs will fall to the Council to fund. There is also likely to be a requirement for capital expenditure on building improvements. It is therefore economically advantageous for the Council to conclude the leases.
  - Approx. 875,000 people use the 3 centres every year, many from less affluent groups within the community. The facilities therefore make a significant contribution to assisting residents, particularly those who may not be able to afford to use private health clubs, to lead a healthy lifestyle.
  - NLT are in partnership with the Northampton General Practise Alliance and deliver the NHS Health Check programme through the centres, thus helping in identifying health issues at an early stage, and where appropriate delivering interventions. 600 health checks will be delivered through the 3 Centres in the coming year.

NLT have also provided a report prepared by the University of Northampton's Institute for Social Innovation and Impact, which analyses the social value of the work carried out by the Trust. This quantifies the annual value to the wider public sector of NLT's activities as being £3.5m. While this clearly cannot all be attributed to the activities carried out at the 3 premises in question, it does give a clear indication of the social and economic benefits which NLT's operations contribute to the borough.

- 4.2.6 The terms of an FRI lease are such that the tenant is responsible for all building insurances. It is usual for this insurance to be arranged by the landlord and recharged to the tenant as an addition to the rent, but tenants can choose to arrange the insurance themselves.
- 4.2.7 Consideration is being given to whether or not it will be of benefit to NLT for the Council to continue to insure the properties under the Council's block insurance, or for NLT to arrange their own insurance. If it is more cost effective for NLT to insure through the Council's policy, and on the basis that there will be no financial impact on the Council should a claim be made, the full apportioned cost of the insurance will be added to the rent instead of NLT making their own arrangements.

#### Loan or guarantee

- 4.2.8 The proposed new leases will transfer significant additional liability for repairs, maintenance and improvements of both the buildings and the plant from the Council to NLT. To meet these liabilities NLT has a funding requirement of up to £3m over the coming years. To fund this they will either borrow from the council at commercial interest rates, or they will borrow from a third party with the Council acting as guarantor for the loan.

#### Financial Risks

- 4.2.9 The Chief Finance Officer will undertake all required due diligence and ensure compliance with the Council's Loans Checklist before any loans are made or guarantees provided.
- 4.2.10 NLT have shared their five year financial forecasts with LGSS Finance – these forecasts demonstrate healthy surpluses. Much of the proposed investment in the centres will improve energy efficiency and make savings in utility costs through the installation of Combined Heat and Power (CHP) units and energy efficient lighting.
- 4.2.11 Any loan would be secured on the leases, (although this may not provide full 'security' value) therefore if the Trust were to default on loan repayments the Council could take back direct control of the leisure centres and would realise the ongoing benefits of the investments made. The risk of not providing this loan facility or acting as guarantor, would reduce 'risk' as perceived by loans, but through absolute crystallisation of £M costs that NBC would have to incur to maintain and replace the Plant, Equipment and Facilities that the Leisure Trust propose to use these fund for.
- 4.2.12 Any loan will be made by the Council at commercial interest rates in line with State Aid rules and taking into account the level of risk. This is currently expected to be in the region of 4.5% to 5%. The loans may be funded by borrowing from PWLB, at a rate of between 2% and 2.5%. If these rates remain the Council will generate surplus interest of up to £0.050m per annum over the period of the loans. The interest earned will exceed our current 'deposit rates' of c0.45%

- 4.2.13 The 2018/19 General Fund revenue budget, as approved by Council on 26<sup>th</sup> February, includes rental income of £50k per annum from NLT.
- 4.2.14 The Council will also make savings on ongoing repairs and maintenance and insurance costs, responsibility for which will pass to NLT. The average expenditure on repairs and maintenance over the last 3 years has been £0.019m.
- 4.2.15 The Council's capital programme does not include any provision for major repairs or enhancements to the Leisure Centres. The proposals within this report will remove the risk of the Council having to identify funding for such works over the next 30 years. Over the 30 years this could exceed the £675,000 undervalue/discount.

### **4.3 Legal**

- 4.3.1 The Council have sought external legal advice to consider whether there are any procurement law, Section 123 (Local Government Act 1972) or State Aid implications arising from the implementation of the proposed arrangements for the future provision of leisure services (noting the external legal advice excludes the proposed loan and guarantee facility), the key points for the Council to consider are as follows:
- 4.3.2 The Council is under a general duty to achieve best value from the disposal of its land and property arising under Section 123 of the Local Government Act 1972. Circular 06/03 provides a specific consent as set out in paragraph 4.2.5 of this report. The legal advice has stated the grant of a lease at an undervalue may create a State Aid risk i.e. confers an advantage to NTL. The question for the Council is whether this "distorts or threatens to distort competition" and "affects or is capable of affecting trade between the member states". On the basis NLT operates in a very localised area and the services are of a local nature for the people of Northampton it is unlikely trade between member states is affected and therefore State Aid is unlikely to apply; and
- 4.3.3 The Operating Agreement provided by NLT in the view of the legal advice operates as a concessions contract pre the 2016 concessions regulations. On the basis that there is unlikely to be cross boundary interest there is no regulatory requirement to follow any particular process in varying the operating agreement, however any variations should not be significant and should not give the appearance of an entirely new arrangement. In relation to the proposed amendments referred to in paragraphs, 2.4, 2.5 and 2.6 of this report they do not have a significant impact on the operation and variation of the operating agreement.
- 4.3.4 The Localism Act 2011 provides local authorities with wide and facilitative powers to act in the same way as any other legal person, save where those powers are specifically limited by statute (referred to as the General Powers of Competence). The making of a loan or provision of a guarantee would be permissible, subject to any relevant statutory regulations being met. The arrangements must be robust in respect of repayment of any loan to ensure the Council meets its fiduciary duties and has security in place to cover the position of default. The interest rate of any loan will require that the European reference rate methodology be applied to ensure the loan is at a commercial

rate. The Council will need to appoint external legal advisors to draft the loan agreements and/or guarantees as appropriate.

4.3.5 In summary, the external legal advice for implementing the recommendations of this report are low risk but an element of risk will always remain and Cabinet should be aware of this.

#### **4.4 Equality and Health**

4.4.1 Services to the public will be unchanged as a result of the recommendations of this report. There are therefore no direct equality or health implications.

#### **4.5 Consultees (Internal and External)**

4.5.1 Extensive consultation has taken place with NLT in developing the recommendations of this report. Independent valuers' advice has been taken in determining the appropriate level of rent to charge NLT.

#### **4.6 How the Proposals deliver Priority Outcomes**

4.6.1 This report will contribute to the priority corporate outcomes of

- Enhancing leisure activities for local people and encouraging participation and
- Delivering quality modern services

### **5. Background Papers**

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Operating Agreement between NLT and NBC

General Consent Order (06/03)

Valuation from Underwoods

Advice from Browne Jacobson Solicitors (Confidential & Legally Privileged)

Social Value Study from University of Northampton Institute for Social innovation and Impact

**Contact:** Rick O'Farrell, Senior Regeneration Consultant  
rofarrell@northampton.gov.uk