

Report to: Communities Committee, 25th January 2023

Report of: Corporate Director – Operations, Homes & Communities

Subject: MANAGEMENT OF FREEDOM LEISURE CONTRACT 2023/24

1. Recommendations

That the Committee:

- 1.1 Notes the contents of this report and in particular the additional £585,000 unbudgeted costs associated with operating the contract during 2023/24, primarily relating to energy;**
- 1.2 Notes the findings of the Leisure Contract Options Appraisal undertaken by Sports & Leisure Consultancy as set out in this report and within Private Appendix 1;**
- 1.3 Approves £40,000 annual cost reduction measures as specified at Appendix 1 for implementation as of 1st April 2023;**
- 1.4 Recommends to Policy & Resources Committee a capital allocation of £550,000 to undertake energy efficiency works as specified within this report, and included at Appendix 2;**
- 1.5 Notes that a further report setting out a full and detailed business case for the capital investment referred to in recommendation 1.4 will be presented back to this Committee in June 2023;**
- 1.6 Recommends the draft Freedom Leisure Fees & Charges 2023/24 for approval to Income Management Committee, included at Appendix 3;**
- 1.7 Recommends to Policy & Resources Committee the approval of up to £315,000 in financial support for 2023/24 to Freedom Leisure which has been built into the draft budget for 2023/24;**
- 1.8 Notes that open book account meetings will continue to be held in order to reconcile the level of financial support required by Freedom Leisure, up to the maximum value specified in recommendation 1.7.**

2. Background

- 2.1 At its September 2022 [meeting](#), Policy & Resources Committee approved £255,000 revenue funding (to be taken from the Business Rates Risk Reserve) to support Freedom Leisure with additional 'in-year' energy costs that had not been budgeted for within the original contract tender bid. This decision was taken in advance of**

Freedom Leisure needing to enter into new energy contracts for gas and electric in during autumn 2022.

- 2.2 Within the report on this subject, it was forecasted that additional unbudgeted energy costs for 2023/24 were likely to be in excess of £500,000. Freedom Leisure have now forecasted that these additional costs have risen to £585,000.
- 2.3 The report also informed Members that following the agreed withdrawal of an 'in-year' fees & charges proposal from Freedom Leisure, that a proposal to increase fees & charges in the region of 13-15% would be tabled ahead of 2023/24 in order to try and meet a proportion of the additional costs faced.
- 2.4 In noting the report and in particular the commitment for the Council to undertake a full options appraisal and recommendations for operations and future funding, Members of the Committee signalled that continuing to fund 100% of Freedom Leisure's additional unbudgeted costs was not sustainable and that all options should be thoroughly investigated, even those that had historically been considered difficult.
- 2.5 Following the Committee, Sports & Leisure Consultancy (SLC) were commissioned to undertake a contract review. The full SLC Contract Review is provided in **Private Appendix 1** to this agenda. This report summarises the findings and recommendations of the SLC Contract Review which focussed on 5 areas in particular, these being –
 - National state of leisure sector
 - Financial assessment of contract
 - Assessment of Freedom Leisure cost reduction proposals
 - Management options appraisal
 - Assessment of Freedom Leisure's contract extension proposals

National State of Leisure Sector

- 2.6 The leisure market continues to recover from the impact of the COVID-19 Pandemic and in particular the periods of closure or partial restrictions. As a result, many leisure contracts which are not receiving local authority support are running at a loss for those operators. Several smaller leisure trusts have gone out of business.
- 2.7 The recovery has more recently been impacted by the cost-of-living crisis, as a result of a significant increase in energy costs coupled with many people having less disposable income to spend on leisure. Nationally, the leisure sector has also faced a recruitment and retention challenge which has seen operators having to increase salaries.
- 2.8 Market intelligence confirms that nationally, no public authority leisure contracts have returned to pre-pandemic performance levels, leading to either operators or Council's carrying additional costs or taking on additional risk.
- 2.9 Many leisure contracts which prior to the Pandemic and cost of living crisis provided significant management fee payments are now requiring a subsidy. Similarly, leisure operators are reducing their risk exposure to energy, repairs and maintenance. Those operators still actively bidding for contracts are seeking more elements of shared risk with councils to meet their revised risk profile.

2.10 Income levels for health & fitness have not received to pre-pandemic levels, nationally plateauing at 80-85%.

Worcester City Freedom Leisure Contract Recovery

2.11 In respect of the Worcester City Freedom Leisure contract swimming lessons and casual swimming recovery has performed exceptionally well, surpassing pre-pandemic levels of demand. Income from swimming lessons has increased by over 200% with casual swimming income having increased by around 100%.

2.12 However, health & fitness, which is the contract's most significant income stream, remains well below pre-pandemic levels with recovery at Nunnery Wood being slowest (55% at April 2022) and St Johns performing best (72% at April 2022).

Financial Assessment of Contract

2.13 SLC reviewed Freedom Leisure accounts for 2019/20 given this was the most recent period of 'business as usual' and compared this to 2020/21 to understand the contract's overall performance and recovery.

2.14 A "shadow bid" has been developed which estimates the base value of the contract based on pre-pandemic 2019/20 income and expenditure information provided by Freedom Leisure. Development of a shadow bid is a type of benchmarking process which provides an understanding of the likely market value of the contract which can inform understanding of future affordability and assist with medium term financial planning.

2.15 Several income and expenditure assumptions have been made by SLC which are set out in Section 3.2 of their report.

2.16 The key findings of the shadow bid assessment are as follows –

- Income will continue to grow to circa £3.28m compared to £3.13m in 2021/22 but is not expected to return to pre-pandemic levels of £3.60m.
- Health & fitness income is expected to be £460k less than pre-pandemic levels
- Total expenditure will continue to increase to circa £3.43m compared to £2.82m in 2021/22, over £500,000 more than in 2019/20.
- Utilities expenditure is forecast to be circa £523,000 more than 2021/22
- Staffing costs forecast to be circa £73,000 more than 2021/22.

2.17 Further information on the outcome of the shadow bid is contained at paras 1 – 6 of **Private Appendix 2**.

Assessment of Freedom Leisure's Cost Reduction Proposals

2.18 Several cost reduction proposals have been submitted by Freedom Leisure which have been appraised by SLC and these range from cessation of services, through to

capital investment, to increase use of renewable energy. These can be found at Section 4 of the SLC report and includes –

- Reduced operating hours at Nunnery Wood Sports Centre
- Remove Worcester City Active Communities Manager
- Reduced operating hours at Perdiswell Leisure Centre
- Capital investment to increase use of renewable energy
- Closure of St Johns Sports Centre

2.19 This report recommends that Members consider the 2 proposals that relate to reduced operating times at both Perdiswell Leisure Centre and Nunnery Wood Sports Centre which will have the impact of reducing Freedom Leisure's cost base by around £40,000 per annum. The Council would expect all of this reduction to offset the additional costs of energy in 2023/24, forecasted to be £585,000.

2.20 Further discussions with Freedom Leisure have developed these 2 proposals (**Public Appendix 1** of this report), the key elements of which are below –

- Reduce operating hours at Nunnery Wood Sports Centre and apply new operating hours of Mon-Thurs 1500-2200, Friday 1500-2100 and Saturday and Sunday 0800-1300. A reduction of 33 operating hours across a week with cost savings of £32,000 per annum.
- Reduce operating hours at Perdiswell Leisure Centre by closing 1 hour earlier on Mon-Fri at 21:00. A reduction of 5 operating hours across a week with cost savings of £8,000 per annum.

2.21 Freedom Leisure have considered the impact of these 2 proposals and have not identified any particular group of protected characteristics that would be unduly impacted. Impact would of course continue to be monitored and reviewed moving forward as part of regular contract meetings.

Capital Investment to Increase use of Renewable Energy

2.22 During November 2022, information was received from Freedom Leisure regarding what work they had undertaken to reduce energy consumption and what further work could be undertaken. The following is a list of work already undertaken by Freedom Leisure that have contributed to both gas and electricity usage reducing since 2018/2019.

Actions Taken			
All building control systems have been regularly reviewed and changes made	Reduction of pool temperatures	Air conditioning systems off during large parts of the operation	Energy non-negotiables in place and monitored by site and support team.
Installation of Pool cover at Perdiswell	Colleague training and awareness in energy management and Environmental Awareness.	Fitness equipment is turned off whilst not in use	Review of heating/hot water set points
Upgrading to LED lighting	Energy / Environmental action plans in place	Enhanced cleaning of air ducts to ensure consistent flow is achieved	Regular forecasting of energy performance and updates to site management and operational teams
Reduction of low occupancy classes	Appointment of group environmental and sustainability manager	Environmental Boards and additional customer communication on supporting energy saving measures	Ductwork and piping insulation

2.23 Furthermore, during 2022 Freedom Leisure commissioned a study into energy conservation proposals for each of the 3 Worcester sites. These proposals are included at **Public Appendix 2** of this report and include –

- Lighting improvements
- Pool pump controls
- Air handling units
- Solar technology
- Heat pumps

2.24 Having considered the report it is recommended that lighting improvements at each of the 3 sites, pool pump controls at Perdiswell, air handling units at St Johns and solar panels at each of the 3 sites are progressed in order to reduce the energy costs associated with each site and in doing so carbon emissions.

2.25 Undertaking this work would require capital investment of around £550,000 (inc. contingencies) and this is broken down below, along with the estimated savings resulting from these works and associated carbon reduction and energy consumption reduction. Estimated savings from all these works is around £147,000 per annum with partial payback commencing after 1.6 years (lighting works) and full payback after 3.9 years (solar panels). These measures are unlikely to deliver any savings during 2023/24 but subject to approval of this report would be considered when developing the medium-term financial plan.

Site	Measure	Estimated Project Cost (£000')	Estimated Annual Saving	Estimated CO2 reduction (te)	Estimated energy reduction (kWh)	Payback Period (years)
Perdiswell	Install high efficiency internal and external lighting	6.5	3.9	1.5	7,245	1.6
Perdiswell	Install new pool chemical dosing system and controls	80.6	25.4	10	47,024	3.2
Perdiswell	Install solar panels	122.9	34.3	13.5	63,500	3.6

Total		210	63.6	25	117,769	
St Johns	Install variable speed drives to air handling units to vary output based on demand	15.6	8.3	3.2	15,304	1.9
St Johns	Install high efficiency internal and external lighting	5.7	3.2	1.3	5,903	1.8
St Johns	Install solar panels	122.9	32.7	12.9	60,520	3.7
Total		144.2	44.2	17.4	81,727	
Nunnery Wood	Install high efficiency internal and external lighting	27.0	8.9	3.5	16,418	3
Nunnery Wood	Install solar panels	119.0	30.2	11.9	55,950	3.9
Total		146.0	39.1	15.4	72,368	
Total for 3 Sites		500.2	146.9	57.8	271,864	

- 2.26 At this stage, progressing with air heat pumps has not been recommended as, although this measure would reduce gas consumption at each site, it would at the same time increase electricity consumption. Although a net reduction of energy consumption and carbon emissions would still be likely, there would be little or no cost savings due to the current cost per kWh of electricity being more expensive than gas. Ofgem's price cap rates as of 1st October 2022 confirmed that gas had gone up to 10.3p per kWh (from 7p) and electricity had gone up to 34p per kWh (from 28p).
- 2.27 Further discussions are required before these schemes are progressed to full and detailed business cases, but it would seem prudent for the council to invest in these capital improvements as the landlord and ensure by agreement that all financial benefits associated with the improvements are received by the council.
- 2.28 At this stage therefore, it is recommended that an allocation of capital is approved for inclusion within the capital programme, but its release would require a full and detailed business case being presented back to this Committee and Policy & Resources Committee for approval.

Management Options Appraisal

- 2.29 SLC have undertaken an appraisal of the primary options available to the council for the future management of its leisure services. These include:
- In-house management

- Local Authority Trading Company (LATC)
 - Management by multi-site trust operator ('as is')
- 2.30 The approach taken to appraise these options is in line with Sport England's Leisure Services Delivery Guidance and includes establishment of a pre-set of defined criteria (financial and non-financial) based on Council priorities and agreed with officers, development of a financial model which sets out relative income and expenditure projections for each model, and assessment of each model against both financial and non-financial criteria.
- 2.31 The evaluation criteria applied and appraisal assumptions for each model are at Sections 5.2 – 5.3 of the SLC report.
- 2.32 The financial modelling clearly indicates that the current management model of management by a multi-site trust operator would be the least expensive for the Council as set out in the SLC report. The most expensive management model is that of 'in-house' which it is estimated would cost the council in the region of £1.286m per annum. It is estimated that running the council's leisure service through a LATC would cost in the region of £735,000 per annum.
- 2.33 Operating the service in house would result in a reduction in income of around 7% as the council would not have the sales, membership and communications expertise that a leisure trust operator carries. Additionally, an in-house model would raise the cost base significantly as a result of reduced purchasing power and economies of scale, local authority terms and conditions (including pension costs) and higher support service costs as it would not be possible to share these across contracts. Further information is provided at para 7 of **Private Appendix 2**.
- 2.34 These disadvantages would also apply to a LATC delivery model, albeit to a lesser extent as, for example, staff would not be operating under local authority terms and conditions or benefit from the local government pension scheme and tax recovery would be more efficient.
- 2.35 Non-financial factors were also appraised and there was less of a distinction identified, which illustrates Freedom Leisure's commitment to supporting the Council with its City Plan aspirations particularly around health & well-being.
- 2.36 In addition to the appraisal exercise undertaken, SLC have also identified one-off costs associated with mobilising a new service in a 3-month period and these are set out at Section 5.4 of the SLC report. Mobilisation costs range from around £125,000 for a LATC up to £140,000 for 'in-house' transfer. It is more realistic, however, to consider mobilising over a longer period, perhaps up to 6 months which would increase these costs by up to double potentially.

Assessment of Freedom Leisure's Contract Proposal

- 2.37 The Council's contract with Freedom Leisure is due to end in October 2025 which, with less than 3 years to run, is why officers have started to consider what a preferred option may look like for delivering future public leisure services in Worcester City.

2.38 As a valued partner delivering an excellent service, but also as part of assessing how best to manage the additional costs associated with the existing contract linked to the increase in energy prices, discussions have commenced around the option of a contract extension. Further information is provided at para 8 and 9 of **Private Appendix 2**.

Draft Fees & Charges Proposal 2023/24

2.39 The draft fees & charges proposal submitted by Freedom Leisure is included at **Appendix 3** of this report.

2.40 The average increase in fees & charges across all activities is 8.8% compared to CPI inflation which in November 2022 was running at 10.7%.

2.41 Many activities are proposed to have zero increase applied and these include –

- Swimming galas
- Swimming for children under 16 from priority wards during specific school holiday sessions
- Unsupervised bookings for whole main hall at Perdiswell, St Johns and Nunnery Wood and half main hall at Perdiswell
- Pay as you go health & fitness
- Squash league joining and renewal fees
- Equipment hire (inc. replacement cards)
- Supervised multi-sports party
- Pay & play tennis (exc floodlights)
- Private tennis lesson

2.42 Where increases in membership packages are proposed these range from 7.78% (Connected Worcester Junior) to 13.34% (Freedom Swim) with average increase in this category being 10.16%

2.43 In respect of Swim School increases proposed range from 13.48% (45-min swim lesson) to 13.48% (60-min rookie lifeguard) with average increase of 13.7%.

2.44 In respect of other swimming activities increases proposed range from 11.1% (Under 4 swim) to 100% for an over 75 annual swim pass which is currently priced at £10.00.

2.45 It is proposed to increase school swimming fees on average by 12%. For clubs and private hire increases of 7% are proposed for the main pool and teaching pool (exc gala's).

2.46 Freedom Leisure have pre-agreed (September 2022) prices with Worcester Swim Club and these are included within the proposal for completeness.

2.47 In respect of specialised swimming sessions increases proposed range from 6.7% (2 to 1 private swimming lesson) to 14.3% for an over 50 swim with average increase of 10.6%.

- 2.48 In respect of unsupervised activities increases proposed range from zero (7 out of 13) to 11.5% (premium rate weekday squash) with an average increase of 2.5%.
- 2.49 In respect of supervised activity increases proposed range from 3.1% (short mat bowls) to 12.5% (fitness classes at St Johns Sports Centre) with an average increase of 6.6%.
- 2.50 In respect of artificial grass pitch's and athletics track increases proposed range from 4% (artificial grass pitch's at all centres) to 10% (athletic meets and club hire).
- 2.51 In respect of tennis, increases of over 9% are proposed to membership options. Charges for use of floodlights at tennis courts are proposed to increase by 10%. Increases of 30.34% are proposed for a junior 30-minute group session which is currently charges at £4.45 with adult group sessions proposed to increase by 4.48%
- 2.52 The additional income that would be generated from this fee & charges proposal would be in the region of £230,000 and the council would expect that all of this additional income would contribute to offsetting the additional costs relating to energy in 2023/24 forecast to be £585,000.

3. Preferred Option

- 3.1 This report has been developed having considered the findings and conclusions of the SLC contract options appraisal report, which was a piece of consultancy work commissioned by the council in order to advise on the most appropriate means of managing the remaining period of the contract through until October 2025.
- 3.2 In order to ensure the ongoing provision of leisure across the council's 3 sites the preferred option of this report includes the following –
- Approval of a set of fees & charges increased broadly in line with inflation, that will raise additional income in the region of *£230,000 per annum*;
 - Approval of cost reduction measures that include a reduction in operating hours at 2 sites that will reduce operating costs by around *£40,000 per annum*
 - Recommends a capital allocation of £550,000 in order to install energy reduction measures across all 3 sites that will within 4 years deliver financial savings in the region of *£147,000 per annum*
- 3.3 Approval of these measures will contribute to reducing the additional £585,000 in unbudgeted energy costs faced by Freedom Leisure in 2023/24 but is still likely to result in an operating deficit of around £315,000.
- 3.4 With the SLC report indicating that the other options are likely to be significantly more expensive, the preferred option is to provide Freedom Leisure with financial support up to £315,000 in 2023/24 (via an ongoing open book arrangement), so that the provision of leisure out of the council's 3 centres and via its Active Communities programme is safeguarded.
- 3.5 It should be noted that the level of Government support available to the leisure sector is uncertain and so any assumptions that have been made by Freedom Leisure in respect of ongoing financial support in 2023/24 from Government, may require

'in-year' review as part of ongoing open book arrangement, should that funding support not be made available. This will of course be presented to Members of this Committee and Policy & Resources Committee should this be the case.

4. Alternative Options Considered

- 4.1 As outlined in this report, the option of providing 100% financial support to Freedom Leisure to support them with increased energy costs has been discounted following Policy & Resources Committee in September 2022.
- 4.2 In respect of energy reduction measures, capital investment in heat pumps at the 3 centres has been discounted on financial grounds as potential savings from gas costs would be offset by increased by an increase in electric costs, which is priced significantly higher at this current time.
- 4.3 The provision of accessible and reasonably priced leisure, health & well-being opportunities to Worcester residents is significantly important as set out in the City Plan and as illustrated through planned and delivered projects including the Nunnery Wood Levelling Up Bid, Perdiswell Artificial Pitch Project, King George V Artificial Pitch Improvements and the Artificial Cricket Wicket at King George V Playing Fields. Therefore, putting this provision at risk by not providing subsidy support to Freedom Leisure has been discounted having regard to the national and sector insight provided through the SLC report.
- 4.4 Given the extent of the financial challenge faced by Freedom Leisure, which the Council has become exposed to, it has become necessary to consider where operating costs can be reduced. This report recommends a reduction in operating hours at Perdiswell Leisure Centre and Nunnery Wood Sports Centre and such a reduction can be mitigated by the fact that there are 3 sites in operation with each of these sites open every day of the week.
- 4.5 The option of completely closing one or more centres has been discounted as financially any savings from closing a site would be offset by a reduction in management fee owed to the council, and in addition there would be additional costs associated with closure including HR costs and site management costs that would need to be picked up by the council.
- 4.6 Furthermore, completely closing one site, even if temporarily risks sending out a negative message both about the councils commitment to leisure, health and wellbeing and more so to that site in question.

5. Implications

5.1 Financial and Budgetary Implications

The implications of revising the Leisure operations and the fees & charges schedules are set out in the report. The current budgeted income derived from the Management fee is £520,000 per annum. It is proposed to maintain that income stream in the MTFP in the short term and to offset the increase in costs by way of a financial contribution to the Freedom Leisure. This provides for transparent cashflows and enables the Council to continue to see the impact of financial pressures on the contract in line with existing arrangements. It also allows for a degree of risk-sharing in respect of costs which can be assessed using the open book approach.

The draft MTFP presented to Policy & Resources Committee in December 2022 included an estimated increase in energy costs of £523,000. This report indicates an estimated increase of £585,000, mitigated by increased fee income of £230,000 and efficiency measures of £40,000. Assuming that these mitigations are achieved, and applied in full, the impact on the MTFP will be £315,000, reducing the estimated budget gap by £208,000.

5.2 Legal and Governance Implications

Subject to approval of this report, financial support would be managed and provided on the same basis as during the COVID-19 Pandemic via a fully open-book arrangement with payments made in arrears.

There is no clear provision within the contract that is required to be triggered for this support to be put in place and the arrangement is very much in the spirit of the contract being a partnership arrangement.

5.3 Risk Implications

There are 2 corporate risks linked to this report, namely –

- City Plan Priorities – Financial Resources
- Leisure Centre Operations

As has been set out within this report, continuing to operate via the existing contract arrangement with Freedom Leisure (that sees us receive an annual management fee of more than £500,000) is the best value option.

It remains the best value option even during this extended period of having to provide additional financial support, as there is still a net benefit position to the council.

Continuing to operate in this way ensures the council does not have to further deplete its reserves or require cost reduction measures having to be applied in statutory and non-statutory critical services. The proposal therefore addresses the Council's overall risk of not having sufficient resources to deliver the City Plan and its statutory functions.

The leisure centre operations risk acknowledges the risk to the viability of the Leisure Operator due to the continued increase in costs and the return of demand being impacted firstly by COVID-19 and exacerbated by the cost of living crisis.

The recommendations contained within this report (subject to approval) will ensure that Freedom Leisure continue to operate a successful contract across Worcester City and address this particular risk.

5.4 Corporate/Policy Implications

The Worcester City Plan 2022 – 2027 makes it clear that Worcester aspires to be a healthy & active city where people should have the opportunity to be as fit and healthy as they can be by using all of Worcester's assets, from the swimming pools to our green spaces, to improve their wellbeing.

Part of this is people using state-of-the-art fitness and leisure facilities provided by Freedom Leisure on behalf of the Council, to be active and healthy.

The Council wishes to help more people make healthier choices, more easily leading to an increase in sport and physical activity for all age groups through the wider sporting community, such as the Parkrun and grassroots sport.

5.5 Equality Implications

Having considered fully the recommendations within this report having regard to equalities impact, no implications have been identified. The area that could present most risk from an equalities point of view is that of the proposed reduction in operating hours across 2 of the sites.

Freedom Leisure have interrogated their activity and classes schedule and have identified that no group of protected characteristics will be impacted by the proposals.

5.6 Human Resources Implications

As touched upon in the 'Management Appraisal Options' section of this report, should the council at this stage or in the future take a decision to close one or more centres which, then consideration would need to be given to Transfer of Undertaking (Protection of Employment) Regulations if there were Freedom Leisure staff working on the Worcester contract who transferred over from the Council at contract commencement.

Furthermore, for those staff who would not be captured by TUPE but who would be made redundant because of a centre closing, there would be both notice pay and redundancy costs that would require to be covered with a decision to be taken on which party picks these costs up.

5.7 Health and Safety Implications

There are no health and safety implications associated with this report

5.8 Social, Environmental and Economic Implications

Subject to approval of this report there would be broadly positive social, environmental, and economic implications.

Socially, sustaining the operation of the Council's three leisure centres and the active communities programme will benefit the health and well-being of our residents and users both physically and mentally.

Environmentally, the increase in energy prices to such an extent has added emphasis and pace to the commitment that was already in place to consider alternative power generation across the three centres. It will also drive the day-to-day operation to further consider how energy consumption can be reduced.

Economically, sustaining the operation of the Council's three leisure centres will ensure that locally-employed staff remain employed and furthermore will ensure that the leisure market remains competitive with a thriving public sector offer.

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Background Papers: None