PART 2 – CONFIDENTIAL FACTS AND ADVICE

MD2910
Title: Crystal Palace National Sports Centre refurbishment and operator contract

Information may have to be disclosed in the event of a request under the Freedom of Information Act 2000. In the event of a request for confidential facts and advice, please consult the Information Governance team for advice.

This information is not suitable for publication until the stated date because:

This paper contains commercially sensitive information that would distort genuine competition for the future tendering process for both a new operator for the centre and for the procurement of a contractor for the capital works should the project progress. This would prejudice the commercial interests of the GLA and is not in the public interest.

This Part 2 also contains legal professional privileged advice.

Date at which Part 2 will cease to be sensitive or when this information should be reviewed with a view to publication: Review 30 June 2023

Legal adviser recommendation on the grounds for not publishing information at this time:

In the event of any request for access to the information contained in this document and/or its appendix under section 1 of the Freedom of Information Act 2000 (the Act), it is considered that access can be denied on the basis that the information constitutes exempt information under:

- section 42 of the Act on the basis that part of the information contained in this Part 2 is legally privileged
- section 43 of the Act on the basis that disclosure of the information in this report would prejudice the commercial interests of the Authority, as its release could have an adverse impact on the Authority's ability to secure best value through future procurements that it may undertake in relation to the Crystal Palace National Sports Centre (CPNSC) estate.

Section 1 of the Act creates the general right of access, which provides that any person making a request for information to a public authority is entitled:

- to be informed in writing by the public authority as to whether it holds information of the description specified in the request
- if that is the case, to have that information communicated to him/her.

As noted above, section 43 of the Act provides that information is exempt information if its disclosure under the Act would or would be likely to prejudice the commercial interests of any person (including the public authority holding it). The paragraph above states that the information could be considered commercially sensitive, as its release could affect the commercial interests of the Authority and its ability to secure best value in relation to future procurements and therefore, is covered by the exemption under section 43 of the Act.

The section 43 exemption is a qualified exemption and, as such, is subject to a public interest assessment.

Public interest assessment
On balance it is considered that the public interest is best served if the information is not disclosed at this point. Disclosure by the Authority could have a detrimental effect on the Authority's procurements and bargaining position; and its ability to formulate a strategy for the optimum future of and investment in the CPNSC and the surrounding site, and the most economically advantageous management of the CPNSC. As a result, the effective delivery of the chosen option might be prejudiced, which in turn might precipitate an increase in the burden on public funds.

For these reasons, it is considered that the information in this Part 2 is exempt from publication in reliance upon the exclusions contained in section 43 (commercial interests) of the Act; and because the public interest in withholding the information outweighs the public interest in releasing it.

Legal Adviser – I make the above recommendations that this information is not suitable for publication at this time.

Name: John Benson **Date:** 28 October 2021

This Part 2 should be read in conjunction with Part 1.

Decision and/or advice:

1.1. This decision seeks approval for GLA expenditure of up to £58m to deliver the comprehensive refurbishment of the CPNSC. The investment will be funded from the capital receipts unapplied reserve and GLA Group business rates reserve. It is intended that external funding will be sought to contribute towards the refurbishment costs and therefore seeking to reduce GLAP expenditure.

1.2. The CPNSC is currently a GLAP asset. Advice has recently been sought from Queen's Counsel about the nature of assets held by GLAP. Details are set out in the attached GLAP steering group paper. In the light of this advice and criteria to be developed by officers, this decision form seeks a delegation to the Executive Director of Resources to consider and approve changes to the ownership of CPNSC and or make changes to the contractual structure. As part of the exercise of this delegation advice will be sought to determine the tax implications associated with the GLA investment proposed under this decision. This advice will be used to identify the most efficient budgetary route for the GLA. This includes considering the question of whether it is best to leave GLAP as the owner of the asset and party to the operator contract with GLL or whether it is better to have the asset transferred to the GLA and/or the operator contract with GLL novated to the GLA.

1.3. As outlined in this Part 2 paper, the future ownership of the CPNSC will be determined in light of updated legal advice. Hence any reference to investment in this asset may refer to GLA or GLAP but should be read as the ultimate owning entity, once future strategy has been clarified.

2. Legal issues

2.1. Subject to approval required by this MD, GLA Land and Property Limited (GLAP) proposes to vary the terms of the CPNSC contract for Greenwich Leisure Limited (GLL) to continue to provide the management and operating services under an open-book approach. The total value of the extension remains the same as MD2746 (up to £1.3m per annum (up to £2.6m for the remainder of the contract term up to 31 March 2023)), which is based on the same terms as the previous contract but with a reduced margin, from 5 per cent down to 2 per cent, and a 50/50 split of any surplus from the contract arrangement. Whilst the day-to-day finances are not impacted, the risk for any future large costs currently fall solely to GLAP.

2.2. Under the Concession Contracts Regulations 2016 (the "2016 Regulations"), a re-procurement process should be run as there are no grounds under the 2016 Regulations that apply to allow the CPNSC contract to be varied further. It was awarded in 2004 with an original expiry date in 2009 and has been extended without competition since.

2.3. The proposal to further vary the CPNSC contract carries a risk of procurement challenge for the absence of competition. This is a material variation, moving away from the current terms and, while previous extensions have not been challenged, a challenge on this occasion cannot be ruled out, particularly given (a) previous commitments to a competitive re-let of the contract have not been met; and (b) there is not currently in place a plan for competitive re-procurement.

2.4. While officers believe that it is not appropriate to commence procurement while the future of the CPNSC is uncertain, that approach is not compliant with the 2016 regulations and the risk of procurement challenge remains.

2.5. A successful challenge could result in a court setting aside the extension of the CPNSC contract with prospective effect; imposing a civil penalty at a "dissuasive" level; and possibly awarding damages to the economic operator that made the challenge. A successful challenge could also have a detrimental impact on the reputation of GLAP and, more importantly, the GLA itself.

3. Commercial issues

3.1. A commercial decision is proposed to proceed with the variation, due to the change in the sector post-COVID-19 and the additional risk GLL would retain on a concession-based contract at this time for the CPNSC due to the age of the facility and the likely expenditure required to maintain it.

3.2. Given that approval has already been obtained under MD2746 for an extension, it would seem disproportionate and unwise to re-procure the contract for this variation at this time. Appendix D shows the GLL's high level projection for the CPNSC; based on GLL's current assumptions it is not forecast that it will re-enter a deficit. However this remains uncertain. For further detail please see Appendix F. It should be noted, as set out in Part 1 para 1.21, it is generally accepted that this industry finds it difficult to generate ongoing surpluses.

3.3. As pointed out in Part 1, the main risk for GLAP is any unforeseen financial event that would result in a deficit having to be covered. Whilst COVID-19 restrictions being reinstated remains a risk, the larger risk is a large item failing at the CPNSC and a significant sum of money being required; or, where the money is not spent, the area in question closing as it could be unsafe to operate. This risk is somewhat mitigated by the significant investment being approved under cover of this MD but until refurbishment works are fully completed will remain.

3.4. With regards to the capital expenditure being proposed at CPNSC, Part 1 made reference to the expenditure profile projecting £250k being spent by March 2022. In addition to this, GLA officers project the following annual levels of expenditure (subject to the caveats set out in para 1.27 of Part 1):

Year	Total
2021-22	£250k
2022-23	£5m
2023-24	£32m
2024-25	£20.75m

4. Financial terms

4.1. As mentioned in Part 1, the current projections from GLL anticipate that the operational costs to GLAP will not be any more than that which has already been budgeted for. High level detail is provided at Appendix D for the projections and further detail at Appendix F.

4.2. Negotiations for this variation began with GLL setting out a position that the 5 per cent margin was a red line for it. As discussions progressed, this evolved into the current proposal of 2 per cent, but with GLL receiving an increased share of any surplus funds.

4.3. Reducing the margin and increasing the surplus provides a significant driver for GLL to perform as best it can in the operation of the CPNSC. More efficient delivery of the centre will result in a greater amount of surplus for all involved.

4.4. The following table sets out the current contract liabilities to GLAP compared to those under the variation being proposed:

Item	Current contract terms	Proposed contract terms

London Living Wage Contribution	£70,311.17	Figure released in November 2021 but likely to increase with RPI as a minimum.
VAT top-up	£119,871.40	£120,000
Utilities recharge	£480,000	£480,000
Margin	Fluctuates depending on income. Based on the current projections at Appendix D, should a 5 per cent margin have been applied the average monthly amount would have been £7,500.	Fluctuates depending on income. Appendix D shows current projections. This is an average of £3,000 per month equivalent to 2 per cent.
Repairs	GLL take on costs up to £15,000. Parties jointly responsible for costs between £15,000 and £45,000. GLAP responsible for all repairs over £45,000.	This will all flow through the open-book approach and directly impact the bottom line; and thereby the surplus money taken by each party at the end of each month.
Deficit	GLL takes liability.	GLAP will take liability.
Surplus	All surplus money enters a development pot that is used to improve customer-facing areas.	Each party takes an equal share after agreed expenditure lines have been deducted from the income. This will result in GLAP's overall costs for the CPNSC reducing slightly, but it will not eradicate them.

4.5. The risk for GLAP is where large repair issues are uncovered that were not foreseen in the essential maintenance budget obtained under MD2746, where COVID-19 restrictions are re-implemented, or a separate financial point arises. GLAP would need to cover any costs related to these that exceed any surplus; or to arrive at a different decision where that is not feasible.

4.6. Since April 2020, GLAP has provided the CPNSC with additional funding to ensure its continued operation and maintenance, which totalled £446,400. Of that, £191,142 has not yet been utilised. This sum will be ringfenced up to 31 March 2023 to cover any further unforeseen operational deficits. Any undrawn funds will be repaid to GLAP at the end of the contract.

4.7. Appendix E sets out the finances and shortfall amount that were experienced by the CPNSC and for which GLAP provided funding.

4.8. As of 1 August 2021, projections from GLL indicate that no further forward funding was required. As per the figures at Appendix D, it is not expected that further sums will be required (above and beyond those already committed in the contract, and assuming no COVID-19 restrictions are reinstated).

4.9. The COVID-19 support monies set out above and at Appendix E were arranged via the purchase order system.

5. Finance comments

5.1. Crystal Palace National Sports Centre consists of buildings and leisure facilities, which have reached the end of their economic lifecycle. These assets require substantial investment to improve the buildings and its facilities, to ensure they are safe and fit for purpose. The decision is seeking approval to undertake a comprehensive capital investment programme to improve the CPNSC so that it becomes a fit-for-purpose community asset, generates future savings and reduce the subsidy payable by GLAP.

5.2. An option appraisal was performed by Continuum Sport & Leisure Ltd with Mott MacDonald to consider the most economic and effective option for upgrading the buildings and its facilities, the outcome of each option is included in Part 1, para 1.10 to 1.27. An upfront capital investment of £58m, of which 30% will be allocated to professional fees, asbestos removal, contingency and cost inflation, was considered the most cost-effective option to upgrade and consolidate the buildings and its facilities.

5.3. The upfront investment to upgrade and consolidate CPNSC would provide both social and economic benefits to the community for 25 years. With this option CPNSC could generate an operating surplus of approximately £820,000 per annum, which provides a potential return on GLAP's investment, as concluded by the OBC. However, due to the impact of the COVID-19 pandemic on the leisure industry, the assumptions on cost and revenue were stress-tested and the results showed that CPNSC is more likely to be in a net cost position over the 25 years, see para 1.20 and 1.21 and that GLAP would be required to provide some level of subsidy to fund excess costs.

5.4. The upgrade and consolidate project are expected to commence in 2021-22 and complete in 2024-25, the capital investment of £58m is planned for this period. Preliminary works costing £250k are expected to be incurred during 2021-22, and the remaining £57.750m would be spent in the following three years, with the cost expected to peak in 2023-24 at £32m, as show in Part 1, para 1.28. However, once the detailed feasibility works are undertaken the estimated costs will need to be revisited again, as there is a strong likelihood that there could be significant variance from these initial estimates.

5.5. The decision is also seeking retrospective approval to vary the terms of CPNSC contract with Greenwich Leisure Limited (GLL) up to the end of the contract term at 31 March 2023. The variation would result in an open-book approach being adopted to manage the contract and revision to the financial terms. The variation to the financial terms would result in GLL receiving a reduced margin, from 5% to 2% and an increase in profit share to 50%, with the remaining 50% being allocated to GLAP. The revised financial terms should be an incentive to manage the contract more efficiently.

5.6. A budget for £446,400 was approved in MD2746, of which 57% of the budget has been utilised. The remaining budget of £191,142 will be available until 31 March 2023. Based on GLL's financial plan, no further financial support should be required. However, GLAP has an exposure to the risk of funding costs that may exceed the budget approved in MD2746.

5.7. The potential risks associated with the upgrade and consolidated project were considered and appropriate risks mitigation strategies were identified, see part 1 section 4.

6. Legal comments

Delegation to the Executive Director of Resources

6.1. In exercise of the proposed delegation, the Executive Director of Resources will need to consider the legal advice of Clive Sheldon QC. dated 11 November 2021, a summary of which is set out in the GLAP steering group paper attached to this Part 2.

Further extension of the current operator contract

6.2. This decision form seeks approval of the extension of the current operator contract between GLAP and GLL to March 2023. The legal comments from parts 1 and 2 of MD2746 apply equally to decision 2 of this decision form save that all references to the Public Contracts Regulations 2015 should instead be read as referring to the Concession Contracts Regulations 2016 (the "2016 Regulations"). As has been noted previously, in light of the history of current operator contract, there are no grounds under the 2016 Regulations to justify its further extension. To that end, the decision to extend it involves procurement risk, which has previously been advised on. Therefore, the decision to extend must be made in light of a balance between the known procurement risks of extending the operator contract until March 2023 and the known operational risks of not extending the operator contract.

Retrospective variation of current operator contract to allow for open-book approach

6.3. Decision 3 of this decision form seeks the retrospective approval of a variation to the current operator contract. The variation would introduce an open-book mechanism to the operator contract, whereunder all income and expenditure would be visible to GLAP. Moreover, the Authority would reimburse GLL the sum of any deficit between its income and its expenditure.

6.4. Section 3(4) of the 2016 Regulations sets out the requirements for a services concession contract. Inter alia, a services concession contract must transfer to the concessionaire an operating risk. In the case of the open-book mechanism, all of the operating risk is instead assumed by GLAP rather than by GLL. To that end, it may be argued that, by adopting the open-book approach, the Authority is breaching the 2016 Regulations. However, it should be noted that, whilst this makes the procurement position look worse, it does not give rise to any other risks than those which are already present and have been advised upon. To that end, whilst the Mayor may wish to note this discussion, the decision remains one of balancing the procurement risks with the operational risks as discussed above at end of paragraph 4.1 above.

Appendices

Appendix A - GLL Projections
Appendix B - Shortfall figures
Appendix C - GLA Steering Group Paper of 18 November, 2021, entitled "GLA/GLAP Investment"