

<b>Item No.:</b>	<b>Classification:</b> Open	<b>Date:</b> July 21 2009	<b>Meeting Name:</b> Executive
<b>Report title</b>	<b>Gateway 3 – Variation Decision</b> Leisure Investment and Management Programme: Appointment of Leisure Management Contractor		
<b>Ward(s) or groups affected</b>	All		
<b>From</b>	Strategic Director of Environment and Housing		

## RECOMMENDATIONS

1. That the Executive approves the variation of the Grant Agreement with Fusion Lifestyle Limited (Fusion) for provision of Leisure and Facilities Management services under the new terms set out in this report. The new arrangement applies to the following facilities:
  - a. Camberwell Leisure Centre
  - b. Dulwich Leisure Centre
  - c. Elephant and Castle Leisure Centre
  - d. Peckham Pulse Healthy Living Centre
  - e. Seven Islands Leisure Centre
  - f. Southwark Park Sports Centre
  - g. Surrey Docks Water Sports Centre

## BACKGROUND INFORMATION

2. The varied agreement is designed to run from 3<sup>rd</sup> August 2009 to 31<sup>st</sup> March 2016 or five years from the Final New Services Commencement Date (FNSCD), whichever is the later. The FNSCD is the first date following acceptance of the Practical Completion Certificate (PCC) for refurbishment work at Dulwich Leisure Centre when the new service at that centre can commence. The currently scheduled date for receipt of the PCC for Dulwich is 14<sup>th</sup> January 2011 and the FNSCD should be no more than four weeks after this.
3. For the purposes of financial modelling a seven year contract period is assumed but the significant point is that Fusion require five clear years of operating Dulwich Leisure Centre in its refurbished form in order to fulfil the business plan.
4. The annual cost of the varied agreement is tapered, giving substantial savings on current budget in the later years of the arrangement. The grant is index linked and is likely to vary year on year at RPIx which currently stands at 1.7 %.

## Key Aspects of Proposed Variation

5. Fusion currently has annual Grant Agreements (commenced in 2000) with the Council underwritten by leases to occupy most sites until 2010 (and the Peckham Pulse until 2014). Since Fusion began managing the Leisure Centres in Southwark they have been paid an annual Management Fee in the form of a grant.

6. Fusion also has first right of refusal under the existing leases to manage sites, such as Dulwich and Camberwell which are re-developed whilst they are in occupation. The newly negotiated agreement allows the Council to redeem the current leases from Fusion, occupy the centres for the purpose of refurbishing them and replace the leases with new ones which will be co-terminus with the new grant arrangement and not include future security of tenure.
7. The new agreement includes the following benefits:
  - Significant savings on current budget over the period of the agreement.
  - A new and robust payment mechanism which sets challenging targets and introduces pre-agreed financial deductions for non-performance.
  - An income share agreement which is an incentive for the contractor to perform and ensures that the Council benefits from income over and above current projections.
  - Challenging environmental targets backed up by incentives and sanctions in the new contract.

### **Background of Contract**

8. On 7th April 2000 The Council, entered into a Grant Agreement (the "Grant Agreement") with Southwark Community Leisure Limited (SCLL) for the management of the Council's Leisure Centres. SCLL has since changed its name to Fusion Lifestyle (Fusion). Fusion and the Council are now proposing to vary the Grant Agreement for reasons outlined in the report below.
9. On 13th February 2007 the Executive received a report on the Leisure Centre Investment Strategy. The Council decided to invest £12.3 million of its own capital to refurbish the Borough's existing Leisure Centres. In light of this decision, the Executive asked officers to evaluate all options for management of the Leisure Centres and report the findings back to the Executive. The main purpose of this exercise was to ensure that the refurbishment programme proceeded smoothly with least disruption to customers and to ensure a higher standard of service once the refurbishment was complete.
10. A 'Project Team' comprising officers of the Council and external advisors agreed objectives for the service and a range of options which might achieve these objectives. Each option was evaluated against a set of pre-agreed evaluation criteria and a final score was calculated for each. A soft market-testing exercise was also undertaken by members of the team to see if known contractors in the south east leisure market were interested in taking on Southwark's Leisure Centres prior to and during a process of development. The view from the market was that this would carry a high risk premium and would not be attractive to them.
11. In light, principally of the needs of the refurbishment programme, the highest scoring option was to renegotiate the current management arrangement with Fusion as sole provider and then go to the market of service providers at a future date. If this variation is agreed a new Project Team will be brought together in 2014 to consider progress of the contract and consider options for retendering of the contract when it is due for termination in 2016.

12. The Executive approved this option in the Gateway 1 report “Procurement Strategy for Future Operational Management of Leisure Centres” on July 24th 2007. The Gateway 1 report recommended that negotiation of the new arrangement with Fusion should be based on a minimum of five years and a maximum of ten years.
13. The Executive delegated sign off of the Gateway 2 report to the Strategic Director of Environment and Housing. Due, however, to information that has subsequently come to light the new arrangement is to be treated as an extension of the current Grant Agreement (a Gateway 3 Report) rather than a new contract (a Gateway 2 Report) Under the current Contract Standing Orders, such a variation decision would fall within the remit of the finance director, but in view of the history, complexity and strategic importance of this contract, this decision has been brought back to the executive.
14. Since that time officers have been in negotiations with Fusion over a range of issues and are now in a position to recommend that the extension of the Grant Agreement is ratified.
15. Negotiations have been very complex because the process has been going on in parallel with final negotiations with Buxtons (the Design and Build Contractor for the refurbishment programme) and the planning, design, and scheduling of the building programme for both Dulwich and Surrey Docks Watersports Centres. Dulwich is particularly difficult because of the age and listed status of the building. There were a huge number of unknowns for both the Council and Fusion to deal with such as when to decommission the centre with minimum impact on customer income, staff redundancies etc. This and the date of the final opening of the centre will have a considerable impact on the cost of the service to the Council and the profile of profit and loss over the life of the agreement.
16. Such negotiations would have been impossibly complex if the Council had been through a full tendering process for a new leisure management contractor. The added complexity of trying to transfer the business to a new contractor and redeeming the leases from Fusion (if this had been the outcome) would have added more time and cost to an already convoluted process. This delay and cost have been minimised, if not obviated, by dealing with the incumbent contractor. As it is, Fusion have had to re-profile their business plan several times to deal with programme shifts and new information as it has materialised. As a consequence of the emergent issues, sign-off of the new arrangement has taken almost fourteen months longer than originally envisaged.

### **Context for this variation**

17. Following approval of the “Leisure Centre Investment Strategy” report on 13th February 2007 the Executive approved the Works Procurement Strategy, for the design and build contract, (on 24th April 2007). A procurement exercise followed this latter decision and on 27th March 2008 the Gateway 2 report recommending the selection of Buxton Building Contractors Limited, as the works contractor to undertake refurbishment of the Leisure Centres, was approved by the Strategic Director of Environment and Housing.

18. The refurbishment works will have a major impact on the management of the Leisure Centres and the services provided. Over the next five years some of the Leisure Centres will be fully operational (after the work is completed or pending) and others will be partially open or fully closed for a time as work is undertaken. This will require changes to the current contractual arrangements for the management of the centres, which are based on all centres being fully operational. A procurement strategy for a Leisure Management Agreement was therefore needed to ensure that the management of the centres would enable the building works to proceed efficiently and with minimum disruption and at least additional cost to the Council.
19. In addition to the need to allow the redevelopment of the centres, the Gateway 1 Report, "Procurement Strategy for Future Operational Management of Leisure Centres", identified the key objectives for the procurement strategy as being;
  - Sustained service improvement (including greater innovation and community involvement);
  - Greater Council influence on the service policy and design (i.e. what it looks like and how it is delivered);
  - Improved cost effectiveness and efficiency;
  - Greater transparency through more open book accounting (by the service provider);
  - Greater flexibility to make changes to the service (including the identity of the provider) as necessary;
20. The Gateway 1 rehearsed several ways of achieving these objectives and concluded that the best way was to negotiate a new contract under new terms and conditions with Fusion and all this has been achieved under the proposed new arrangement.
21. In order to ensure best value for the Council the project team considered the options and came to the conclusion that a contract period comprising a minimum of five years to a maximum of ten years should be used as the basis for negotiation with Fusion. This would allow the Council and the contractor to compensate for the loss-making period when the centres were closed for redevelopment by building up the business once they were reopened and having a period of stability in centres that will be refurbished and attractive to larger numbers of customers. With the centres refurbished and the business established, the Council will be in a much better position to attract competitive bids for management of the Leisure Centres. The Council will also have five solid years of benchmarking information about the performance of the centres to compare bids against.
22. Negotiations with Fusion have centred round the ideal length of contract (both for Fusion and the Council), the overall cost of the contract to the Council, the services that Fusion will provide, the sanctions for non-performance and the responsibilities that Fusion will take on.

## **CURRENT POSITION**

23. The Council's negotiation team are now satisfied that all commercial, employment, pensions and policy issues positions are properly resolved.

## **THE TENDER PROCESS**

24. The Executive of 24th July 2007 agreed that the most efficient route for achieving value for the Council would be to enter into single supplier negotiations for an extension of contract with Fusion Lifestyle and therefore the contract was not advertised. At that time it was assumed that this would be a new contract under Gateway 2 protocols rather than an extension under Gateway 3.
25. Fusion was required to submit a Pre Qualification Questionnaire (PQQ) for evaluation by the project team and Southwark Procurement Unit. This was submitted in August 2007 and assessed Fusion's position on the following;
  - Company Information;
  - Financial Information;
  - Equal Opportunities;
  - Health and Safety;
  - Technical Information;
  - Environmental Considerations;
  - Quality Assurance;
  - References;
26. Fusion's initial response was assessed and further clarifications were sought. Once Fusion had provided further information the Council approved the Fusion PQQ as acceptable.
27. Following the assessment of the PQQ, a Request for Proposal documentation was prepared with assistance of the Council's legal, technical and financial advisers and in consultation with the Council's procurement unit.
28. The proposal documentation required Fusion to provide their proposals and detail their experience on the following areas:
  - Sports facilities management expertise
  - Operational competence and effectiveness
  - Acceptability and deliverability of income and expenditure projections
  - Usage projections
  - Investment proposal (e.g. for fit out of refurbished facilities)
  - Management structure
  - Technical merit and capacity
  - A commitment to sustainable work practices
  - Quality Assurance
  - Ability to accept risk transfer (e.g. extent of repairing liability, income projections, utilities costs)
29. Fusion's proposal was evaluated by the project team which included the Council's key advisors on the Leisure and Facilities Management Contract as listed below:
  - Nabarro – Legal advice / compliance
  - Deloitte – Financial advice and assessment
  - Cyril Sweett – Technical advice and assessment
  - LB Southwark client team – Overall assessment

This team was also involved at various times in the negotiations with Fusion which were led by the Southwark Client Team. All those involved in the evaluation and negotiation process have contributed to this report.

### **FUSION'S CURRENT PERFORMANCE**

30. Fusion is currently performing well and meeting the standards as they exist under the current contractual arrangements. There have been issues in the past about Fusion's performance but these have now largely been resolved and Fusion has both grown and changed as an organisation. In 2006 the MORI survey reported that public satisfaction with sport and leisure facilities in Southwark rose by 20%. This was in recognition of Fusion's improved performance. More recent results from the survey continue to demonstrate a small but consistent increase in satisfaction (65% in 2006 and 67% in 2008).
31. Issues which affect customers directly and have in the past led to complaints such as cleaning; building maintenance and customer care have all been largely addressed and continue to improve. Key standards have been met and raised for cleaning and maintenance and targets for all key groups have also largely been achieved. The annual attendance at Southwark's Leisure Centres has now topped 900,000 visits.
32. The officer team at Southwark have also taken note of all the main performance issues that have arisen over the period of the current agreement (including those which are now largely historical). These now form the core of the payment mechanism for the revised agreement. This means that although we are currently confident that Fusion are able to meet standards that will be required of them, there are effective sanctions available to the Council should those standards not be met.
33. Although there have been several formal tests of the current and future robustness of Fusion's business during the evaluation of their proposals it is worth noting that despite the volatility of the current economic climate Fusion's business does not appear to have been adversely affected in the recent months. Customer numbers continue to grow and membership sales are also not in decline. Fusion have taken an active stance in developing products and packages which help to retain the current cohort of members as well as attracting those who now seek better value than the private sector offers.

### **SERVICE TO BE PROVIDED BY FUSION**

34. It is proposed that the contract with Fusion for the management of the Borough's leisure facilities will commence from 3rd August 2009 and be determined either on 31st March 2016 or five years from the Final New Services Commence Date (FNSCD) which should be no later than four weeks from acceptance of the PCC for Dulwich Leisure Centre (currently scheduled for 14th January 2011).
35. Fusion require at least five years of operation in refurbished buildings in order to make the business plan viable. Unless there are considerable delays in the delivery of Dulwich Leisure Centre it is envisaged that the proposed end dates for the new contract should allow sufficient time for the centre to be and up and running and allow Fusion the five clear years of viable business that they require to deliver the Council the savings enshrined in the contract.

36. In order to be manageable for the purpose of this report the financial model is based on a seven year contract commencing in April 2009. Fusion is currently managing the service and is in receipt of a grant which does not differ significantly from the proposed payment in year 1 of the new arrangement. An actual start date in August 2009 will not have a significant effect on current budget and will not affect the end date of the contract.
37. The annual cost of the contract varies over the life of the contract due to the phasing in of the services and facilities. A Leisure Management Fee will be payable each year commencing August 3rd 2009 and will be subject to inflation with effect from 1st April 2010.
38. In common with most, if not all, local authority provided leisure services in the UK activities at Southwark's Leisure Centres are provided at a subsidy and the cost to the customer of a leisure activity is usually much lower than the cost of actually providing that activity. For example, children and people over sixty now swim free in Southwark and there are a variety of other discounts for all target groups for a range of activities.
39. In order to bridge the gap between income from paying customers and expenditure, the Council will continue to provide Fusion with a Management Fee as it does under the current arrangement.
40. The amount paid in Management Fee by the Council for each year of the revised agreement will be fixed at the time the agreement is signed and will only be varied (by mutual agreement) if there is a variation to the service specification. Fusion will bear the risk for shortfalls in income but there is an arrangement for a share in income with the Council if it is overachieved. The onus is on Fusion to make an accurate and informed projection of the shape of the business in future years of the contract and the income-share agreement protects the Council from under-valuation of the future business.
41. In summary, the proposal from Fusion offers the following key features.
42. **Savings** – The annual savings are greater in the later years as the benefit of the proposed investment come to fruition.
43. **Income sharing** – Fusion's income over the life of the contract is modelled in their trading account. If Fusion achieves greater than budgeted income projections then the surplus income is shared between the Council and Fusion in the following proportions.
44. **Energy** - The varied Grant Agreement sets challenging targets for Fusion to minimise energy consumption. These will be reviewed every year and Fusion will have a have an incentive to beat the target (i.e. minimise energy use) or bear the cost of additional use.
45. **Sustainability** – Fusion has signed up to the Council's recycling targets and will work towards environmental accreditation for each of the sites.
46. **Open book Accounting** – Under the varied Grant Agreement the Council will be able to assess how each centre is performing financially, what the income is and what the costs are (direct and overheads).

<b>Surplus Income</b>	<b>Percentage due to the Council (%)</b>	<b>Percentage retained by Fusion (%)</b>
0% to 5% above Projected Income	25%	75%
Between 5% and 10% above Projected Income	30%	70%
Between 10% and 15% above Projected Income	40%	60%
Above 15% of Projected Income	50%	50%

47. **New 'Look and Feel'** – Fusion have agreed to introduce a new look for the Leisure Centres to make the Fusion tag less prominent and emphasise the Council's logo and the site's identity to reinforce the message that they are community facilities. This will be introduced to the centres as the contract is varied and will include amongst other things a new look website, redesigned centre signage and revised marketing material. This has been done in conjunction with Southwark's Corporate Communications section.
48. **Payment Mechanism** – This part of the varied agreement will impose on Fusion deductions for unavailability of facilities or failure to meet performance standards (both in terms of leisure management and Facilities Management (FM) services on a monthly and annual basis). This is designed to deal with any failures in performance and includes, but is not limited to, the most common irritants to clients being items such as cleaning standards, repairs and maintenance; late opening and customer care. Other items of note include the timely provision of information such as user figures and financial information.
49. **New and more robust set of Performance Indicators** – The Key Performance Indicators (KPI's) are incorporated within the Payment Mechanism and support the Services Specification (see Appendix 1) and the varied Grant Agreement. The KPI's provide a performance standard to which the Service Provider has to meet or exceed. If the Service Provider does not perform to this standard then they are subject to a pre-agreed financial deduction.
50. **Greater repairs and maintenance responsibilities** – The varied agreement sees Fusion take on much more extensive repairs and maintenance responsibilities. Under the current arrangement the Council is responsible for maintaining the building structure and major plant and equipment and Fusion is responsible for maintaining fixtures, fittings and decoration. The new arrangement is more effective and straightforward, Fusion is responsible for all regular maintenance. This will ensure that works are carried out in programmed and planned manner and also that any reactive works are actioned swiftly. The Council still retains responsibility for major repairs and for the centres which are not being refurbished in the current phase of development but the routine upkeep of the centres will become Fusion's responsibility and will minimise the work the Council has to undertake.

51. **New initiatives** – A number of new initiatives promoting participation in physical activity have been introduced into the varied Grant Agreement. These directly relate to target groups and are designed to improve health and well-being in the Borough. They include free swimming for the over 60's and under 16's, cheaper access to the gym for the over 60's, free access to Leisure Centres for Looked After Children and free access to Leisure Centres for carers when they are with their clients. This coupled with the requirement for Fusion to continually develop the services should result in a greater number of visits to the centres and contribute to a healthier more active population.
52. **Customer Forums** - The Service Provider will be holding quarterly 'User Group' meetings at each of the sites. The purpose of these meetings is to gain an understanding of users experiences of the facility and to help improve and develop the services offered. The user group will be made up of fairly elected customers from as many areas of the centre as possible. Minutes of each meeting are to be produced and displayed on the customer information board in the reception area of the centre. Failure to hold the meetings and reasonably address the action points will result in a deduction from the management fee.
53. Overall the varied Grant Agreement will set out the requirements from Fusion in a way which accords well with best practice in the leisure market place and will place an obligation on them to perform to high standards or be subject to financial deductions.

#### Payment Mechanism — Further Detail on Purpose and Operation

54. One of the schedules to the varied Grant Agreement is a "Payment Mechanism" which is used to calculate how much Fusion is paid;
55. An "Annual Management Fee" is agreed in advance in respect of each contract year and is derived from a financial model that is agreed with Fusion. The amount agreed will take into account appropriate indexing for the coming year and any variations to the service which have been agreed between the Council and Fusion.
56. Fusion is paid a proportion of this fee monthly. The amount is calculated by dividing the annual Management Fee by 12 and then deducting from that amount various "deductions." These deductions are in respect of any service or performance failures caused by Fusion and act as an incentive for Fusion to maintain the Council's required standards of service set out in the Services Specification.
57. Examples of the deductions that can be levied are as follows;
58. **"Unavailability Deductions:"** "zones" within a facility can be deemed to be "unavailable" because they do not meet the "availability criteria" set down by the Council and a sum of money will be deducted from the monthly management fee due to Fusion. Examples of the requirements for a zone to be available are that the required hot and cold water is available, it is ventilated as required by the Council in the Services Specification and that any pool water has the quality requirements set down in the Council's Services Specification.
59. There are also various zones which have "related zones" so that if a zone is unavailable then other related zones will also be deemed to be fully or partly

unavailable (whether or not they are in fact unavailable) – for instance if the pool changing rooms are "unavailable" then the pool itself will also be deemed to be partly unavailable and deductions levied accordingly. This is in recognition of the fact that there are some zones which are critical to the running of other areas of the facilities.

60. **"Monthly Performance Deductions:"** These relate to matters such as reporting requirements and planning/programming requirements. Again, if Fusion does not undertake these tasks in accordance with the requirements of the Services Specification, there will be further deductions from the monthly management fee.
61. **"Annual Performance Deductions"** If Fusion cannot achieve and maintain Quest Accreditation or meet requirements in relation to participation targets, deductions can be levied.
62. If repeated failures occur in respect of the same problem then the deductions levied will be "ratcheted" – i.e. increased further. This is to incentivise Fusion to deal with problems as soon as possible and not let them recur.
63. The maximum amount of deductions that can be levied in any contract month is the gross Monthly Management Fee (i.e. the Annual Management Fee divided by 12) for that month. This is based on a pre-agreed schedule of deductions for non-provision of service.
64. There are various obligations on Fusion to monitor its own performance and report any issues where it fails to meet the required standards. There are time limits within which these notifications need to take place and also time periods within which the "default events" have to be contained and/or rectified. The containment and rectification times depend on the priority of the event that has occurred – events with a higher priority have to be dealt with more quickly than those with a low priority.
65. There are various "excusing causes" which mean that whilst there is a technical "failure" no deductions are levied. For instance, if the failure is caused by the Council breaching its obligations under the varied Grant Agreement or if the failure was caused by Fusion acting on the Council's instructions, or if an area is unavailable because of a defect in any of the new buildings or a latent defect in any of the existing buildings (for which the Council is responsible and which has not been caused or contributed to by Fusion), then Fusion would be entitled to state that it is excused from the deduction applying.

### **Utilities**

66. Fusion will be responsible for the purchase of utilities, using the tariffs negotiated by the Council. Consumption targets have been set for each type of utility and for each facility. These are renewed annually and can be adjusted by the two parties. Fusion bears the risk of any variation between the actual use of utilities and the annual target. The Council bears the risk of any tariff adjustment during the year. An adjustment will be made at the end of each year to reflect any variation in tariff price.

### **Property Issues**

## Leases

67. Fusion currently has leases which for most of the centres expire in 2010. The gym at Peckham Pulse is the exception as this expires in 2014.
68. As part of the variation Fusion will be surrendering their existing leases and granted a new lease for each of the facilities from the Authority to enable them to carry out the Services. The leases will exclude security of tenure.

## Leisure Investment Programme

69. The Leisure Centre Investment Strategy (approved by Executive on 13th February 2007) is to undertake building works at the Leisure Centres with an allocation of £12.3m of Council Capital. On 24th April 2007, Executive approved the works procurement strategy. Since that time a contractor has been appointed.
70. The work will be carried out in phases and the first phase is full refurbishment of Dulwich Leisure Centre and Surrey Docks Watersports Centre and refurbishment of the pool at Camberwell Leisure Centre, provided planning and funding allow Southwark Park Track will also be refurbished in Phase 1. The estimated time for completion of Phase 1 is in the latter half of 2010. Phase 2 involves all the other centres and the scope and timing of works is subject to confirmation of development plans for these sites which will be worked up in conjunction with the Council's Major Projects department.
71. The varied Grant Agreement makes provision for this by allowing the Building Contractor access to carry out the building works and acknowledging that Fusion will be able to provide different levels of service pre, post and during the refurbishment.
72. Under the varied Grant Agreement, Fusion will confirm that it has reviewed the Building Contracts for Surrey Docks and Dulwich (and Camberwell pool) and that, provided the buildings are refurbished to the standards set out in the Building Contracts, they will be sufficient to enable Fusion to carry out the Services as provided in the varied Grant Agreement.
73. During the final negotiations with Fusion the Council has reached agreement on the following:

## **Employment, pensions and policy issues**

74. During negotiations, agreement has been reached on the approach to employment, pensions and policy issues.
75. On employment issues: there will be a TUPE transfer of five Council staff comprising of a Watersports Centre Manager and four instructors all employed to work at Surrey Docks Watersports Centre (SDWC).
76. In April of 2000, the Council agreed to the transfer of its leisure management functions, previously an in house direct-service organisation, Southwark Leisure, to Fusion, a not-for-profit leisure Trust. Six out of the seven leisure facilities operated by the Council transferred at the time but SDWC did not. Instead it

remained as a management agreement between the Council and fusion with the employment of the staff remaining with the Council.

77. Following the approval of the Gateway 2 Contract Award approval – Leisure Investment and Management Programme: Appointment of a Works Contractor, the future of the Watersports Centre is now assured. The Centre is undergoing investment to the value of over £2 million to completely modernise the centre and introduce a wider range of leisure facilities. This means that the five staff at the Watersports Centre who are currently employed by Southwark will be working even more closely with other staff from Fusion (e.g., reception and sales staff, gym instructors, exercise teachers, catering and child-care staff).
78. Following consultation with staff it is proposed that there is a transfer to the management of Fusion. This means that there are clear lines of accountability and management at the centre leading to a safer and more effective operation. This is especially important as the number of services the centre provides increases with a commensurate increase in staff and customers. The nature of the Watersports Centre means that operations must be properly co-ordinated to minimise the risk of accident to staff and customers.
79. The Council has been in discussion with the staff at the centre, Trade unions and Fusion. Agreement has been reached between all parties and this has been incorporated into the Agreement between the Council and Fusion. Fusion has demonstrated a thorough understanding and experience of the TUPE process throughout.
80. Agreement has been reached with regards to the Council's requirements for Trade Union recognition, employees' terms and conditions and policies and procedures. Agreement has been provided on mobilisation and transition arrangements. Fusion has confirmed that terms and conditions will be harmonised for all employees.
81. Fusion has also come to an agreement with the Council's Pensions' team on current and future liabilities for pensions.
82. Fusion has been made fully aware of the Council's policies and procedures (other than those relevant to transferring Council staff). Fusion's offer in relation to policy matters such as equal opportunities and fulfilment of the Council's employment and enterprise strategies has been highlighted and Fusion's offer has been found satisfactory.

### **Financial Implications**

83. The proposed management fee will deliver significant savings over the life of the contract. It is difficult to be objective about value for money as there has been no competitive process. It is only really possible to judge Fusion against the existing cost and service. In this respect the Council expects Fusion to be providing a markedly better service at a lower cost, partly as a result of the opportunities afforded by the refurbishment works. Because most leisure activities are heavily subsidised Fusion's main source of significant additional income is through the sales of membership packages. Their ability to do this will be enhanced, greatly, by the refurbishment works that are currently being undertaken at the Leisure Centres.

84. The management fee, once agreed is set for the period of the contract and can only be varied by mutual agreement (if for example the Council asks for an additional service or to have a particular service reduced.)

### **Plans for Monitoring the Contract**

#### Monitoring by Council officers

85. Council officers will continue to monitor the varied Grant Agreement as they have been doing under the current arrangements. Visits to each site will take place approximately once a month (if not more) paying particular attention to cleaning standards and delivery of customer care against an agreed set of criteria. Regular contract meetings will be arranged and a reporting format and structure has already been agreed.

#### Fusion self monitoring

86. The varied Grant Agreement will require Fusion to carry out self monitoring in relation to the standards set out in the services specification and the terms and conditions of the varied Agreement. There are processes in place to encourage Fusion to be open and honest regarding their performance and penalties to discourage them. Fraudulent or erroneous reporting carries its own penalties which involve automatic default with no rectification period and the ability of the Council to further inspect Fusions records.

#### Council's FM monitoring contractor

87. The Council has engaged White Young Green (WYG) as its approved Facility Maintenance Contractor to ensure the successful delivery of the facilities management services and monitoring of FM records within the Leisure Centres once the new arrangement with Fusion commences. In the varied Grant Agreement the responsibility for full repair and maintenance of the centres passes over to Fusion and WYG have been contracted to monitor Fusion's management of the centres in relation to their maintenance obligations set out in the varied Grant Agreement and Services Specification. WYG are expected to;

- Ensure the Leisure Centres are maintained to such levels of condition and to such specifications as are consistent with principles of good estate management.
- The Leisure Centres are maintained in a manner, which prevents deterioration save for fair wear and tear of any part thereof.
- Ensure that the maintenance carried out at the centres and the centres themselves comply with all applicable statutory requirements and Laws
- Monitor and report on the Planned Maintenance element performed by Fusion.
- Assess requirements for repair and lifecycle works based on both the existing survey reports and issues arising from both planned and reactive maintenance at the centres and provide recommendations to the Council
- Undertake best value reviews on the Fusion procured works for the Leisure Centres and review the Asset Registers maintained by Fusion.

- Review Fusion's Permit to Work systems.
- Interface with the Council's Leisure Department specified Authorised Representatives on monthly basis, interfacing with the monitoring systems currently in place for the Hard FM services and checking records on site for both the Hard and Soft FM services.

### **Key Performance indicators**

88. As part of the reporting process a number of new monthly and annual Key Performance Indicators (PI's) have been added to the varied Agreement and have been tied into the Payment Mechanism where non compliance will mean that Fusion will incur financial penalties in terms of a representative percentage of the monthly or annual management fee. In total 27 PI's (7 annual and 20 monthly) have been introduced and focus on the areas set out below.

- Meeting reporting deadlines both monthly and annually
- Ensuring controlled, quick and effective response to reactive maintenance
- Delivery of appropriate management of planned and preventative maintenance
- Fusion's professionalism in dealing with customer enquiries e.g. telephone calls, complaints and feedback from customer focus groups
- The number of visitors to centres and usage by target groups (e.g. people with disabilities, BME groups, and people under 16 and over 60)
- Maintaining good standards of cleanliness throughout the centres
- Ensuring refreshments are available including healthy options.
- Maintenance of Emergency planning records
- Achievement and retention of quality standards such as QUEST and ISO 9001:2000

### **Client structure**

89. The contract will be managed as part of the function of the Council's Environment and Housing Directorate within the Leisure & Wellbeing Business Unit. Once the varied contract is operational, the client team will provide strategic and policy advice to the Council in relation to matters affected by the varied contract.

90. The team will consist of two Council Officers who will manage the performance and ensure the maximised delivery of the varied contract. They will put into practice the systems to develop, monitor, manage and evaluate performance, in line with the overall purpose of being a 'best practice' client. The team will also be responsible for ensuring that statistical returns to other Council departments and external bodies and partners are completed.

### **Plans for the transition from the old to the varied contract**

91. The Council's officers have been working closely with Fusion over the past months to ensure Fusion's mobilisation plan results in a smooth transition from the current management arrangements to the operation of the varied Grant Agreement. Fusion has produced a comprehensive mobilisation plan and Method Statement for how they intend to ensure that the facilities continue to deliver services whilst managing the changes from the old agreement to the new varied Agreement in a seamless and controlled manner.

## **OTHER CONSIDERATIONS**

### **Community Impact Statement**

92. The new arrangements with Fusion go alongside the Council's £12.3 million pound package of improvements to Leisure Centres. Whilst the latter is designed to make the centres more physically welcoming and to address issues such as DDA compliance, the former sets challenging targets for inclusion and participation by the Council's various target groups (such as people with disabilities; BME groups; older people and children and young people).
93. Fusion and the Council have already worked successfully in the past to try and innovate in this area. The Council now offers free swimming to people under 16 and over 60 (as do a number of authorities) but Southwark also offers free swim inductions to people over 60 as well as gym usage for just £1.00. Other innovations include free access to leisure for Looked After Children and their carers.
94. The new arrangement meets statutory requirements for target groups but also sets challenging targets beyond those to find out what people want and remove barriers to participation. The aim is for Southwark and Fusion to work in partnership to continue to innovate and try and offer better value for people who are in most need of good quality sport and leisure facilities at affordable prices

### **Consultation**

#### **Stakeholders**

95. There has been significant consultation with stakeholders in sport, physical activity and health in conjunction with the Sport and Physical Activity Strategy which is currently being drafted. These stakeholders include: the Council's Children's Services Department (specifically Youth and Education); the PCT; sports clubs and sports volunteers; providers of services for people with disabilities (through the Southwark Pro Active Disabilities Sub-Group); Sport England and Southbank University. Points arising from this consultation have been incorporated into the new agreement.

#### Trade Unions and Council employees:

96. The Council has held regular meetings with its trade unions throughout the procurement process. These have been very productive and a positive understanding has been reached.
97. Staff meetings have also been held at which senior management have briefed the workforce at each stage of the process.
98. The full transfer of staff to Fusion is expected to be complete for 3rd August 2009 for the start of the new contractual arrangement.

### **Sustainability Considerations**

99. The new contract has specific requirements in line with the Council's policy of making Southwark cleaner, greener and safer. Specific performance targets for reducing waste and energy consumption are included with in the contract itself.

100. In addition to a targeted reduction in energy consumption, Fusion has agreed Energy Management plans based on Carbon Trust reports. Fusion has also agreed to deliver the Council's recycling targets and is working on becoming environmentally accredited. Energy targets will be reviewed every year and Fusion will have an incentive to beat the target (i.e. minimise energy use) or bear the cost of additional use.

### **Market Development Considerations**

- I. Fusion is a not for profit organisation
- II. Fusion has between 250 and 500 employees
- III. Fusion has a regional area of activity

### **Resource Implications**

101. The management fee proposed can be funded by the Leisure and Wellbeing budget over the seven years and show significant savings, mainly during the last four years.

### **Staffing Implications**

102. As Fusion is the incumbent provider there are no staff implications apart from those covered in paragraphs 51 to 59 and subject to TUPE transfer.

### **Second Stage Appraisal**

103. Initial financial checks were carried out at PQQ stage. A further financial check has now been completed. The results of which state that In the light of the information available, the overall performance and strength is considered to be sound. The company has, therefore, been awarded a low risk status.

### **Conclusions**

104. The Gateway 1 report for this procurement project identified the key objectives for the procurement strategy as being, sustained service improvement, greater Council influence on the service policy and design, improved cost effectiveness and efficiency, greater transparency through more open book accounting and greater flexibility to make changes to the service. Officers are of the opinion that these objectives have been achieved in the process of negotiation with Fusion.

### **Supplementary Advice From Other Officers**

#### **Strategic Director of Communities, Law & Governance**

105. This report seeks the Executive's approval to the variation of the grant agreement with Fusion for the provision of Leisure and Management Services. Whilst Contract Standing Orders provide that a variation of an existing contract at this value can be approved by the Finance Director, as noted in paragraph 13, this decision is referred to the Executive for approval due to the complexity and strategic importance of the decision.
106. The provision of leisure management services is a Part B service under the EU procurement regulations, and as such, is not subject to the full tendering requirements of those regulations. However recent case law and policy

guidance from the EU Commission has suggested that for all procurements (including below threshold and Part B services) there should be adequate advertising to enable the service markets to be opened up to competition, and there is therefore a need to comply with the Treaty of Rome and basic standards for an award of contract. However the European Court of Justice consider that in individual cases, and particularly where special circumstances apply, a contract award might be of no interest to economic operators located in other Member States, and therefore there is no requirement to apply the primary Treaty standards. This report confirms the particular circumstances relating to this variation and why the services cannot be tendered at this stage. Paragraph 10 confirms the informal soft market investigations undertaken, and the lack of interest in these services at this particular time due to the works required at the Leisure Centres, which demonstrates why officers consider it is appropriate to proceed with this variation and delay the procurement of future services.

107. Contract Standing Order 2.3 requires that no steps may be taken to vary a contract unless the expenditure involved has been included in approved estimates, or has been otherwise approved by the Council. Paragraph 85 of this report details the resource implications.

### **Finance Director**

108. The programmed savings are endorsed by an independent Financial Evaluation report produced by Deloitte. This gives a reasonable assurance that the business plan worked up between the Council and Fusion is robust although the plan does not take into account the impact of any new leisure investment besides that agreed within the current programme. The impact of any future investment strategies on the revenue streams, both income and expenditure, would need to be gauged as and when agreed by the executive.
109. All planned and agreed savings proposals will need to be mirrored within the departmental medium term resourcing strategy.

### **Corporate Procurement**

110. This is a gateway three report seeking a variation to the current grant agreement with Fusion Lifestyle Ltd (Fusion) said variation being one of scope and time as detailed.
111. It is noted that following the approval by Executive in July 2007 of a gateway one report, a far more protracted negotiation than expected has been undertaken, due in part to information subsequently coming to light pertaining to servicing the pension agreement. This in turn has resulted in the submission of a gateway three report, as opposed to the expected gateway two (new) contract award report. A gateway three report would normally be reserved to the Strategic Director or Finance Director for approval. However, on this occasion the report is being returned to the Executive for the reasons stated.
112. The report details the benefits that will be delivered to the Council as a result of the revised agreement, but concedes that a lack of comparable market data has meant a direct best value analysis has not been possible.
113. Whilst there has been historic concern regarding some aspects of Fusion's performance during the current agreement, the report confirms that these areas

have been satisfactorily addressed and are now included in the key performance indicators. The contract management arrangements that will be undertaken both internally and through a new facilities maintenance contract that has been procured specifically for this purpose are also noted.

114. The report details how the revised agreement is deemed to meet the desired service requirements and improvements, and confirms that a review will be undertaken in 2014 to determine future service requirements and how best they can be delivered.

### **Reasons for Lateness**

115. The report was delayed to enable external financial advice and verification to be taken into consideration. The report is urgent as further delay would mean a later implementation of the new contract and delay in future savings and benefits being obtained.

### **Reasons for Urgency**

116. Fusion have allowed the Council access to the leisure centres for the purposes of redevelopment on the proviso that a decision on the future contract is taken before the summer recess. Apart from commitments to their own Management Board, Fusion also have sub-contractors on stand-by for the new contract to whom they have also made assurances that a timely decision, one way or the other, will be made.
117. Delay in implementing a decision will also delay potential benefits and savings from the new arrangement. As well as new performance standards, this also includes investment by Fusion on a refresh and re-launch of the service which is included in the new contract sum.
118. Finally, the Council's Facilities Management Contractor is also on stand-by and has been for several months, pending a decision on when to mobilise.

### **Background Documents**

<b>Background Papers</b>	<b>Held At</b>	<b>Contact</b>
Gateway 1 Report – Procurement Strategy for the future operational management of Leisure Centres.	Environment & Housing, Chatelaine House, 160 Tooley Street SE1 2TZ	Jay Yeats 020 7525 0891

### **APPENDIX**

<b>Appendix number</b>	<b>Title of appendix</b>
1	Service Specification

## AUDIT TRAIL

<b>Lead Officer</b>	Gill Davies, Strategic Director of Environment and Housing		
<b>Report Author</b>	Adrian Whittle, Head of Culture, Libraries, Learning and Leisure		
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<b>CONSULTATION WITH OTHER OFFICERS / DIRECTORATES / EXECUTIVE MEMBER</b>			
<b>Officer Title</b>	<b>Comments Sought</b>	<b>Comments included</b>	
Strategic Director of Communities, Law & Governance	Yes	Yes	
Finance Director	Yes	Yes	
Corporate Procurement	Yes	Yes	
Executive Member	Yes	Yes	
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