

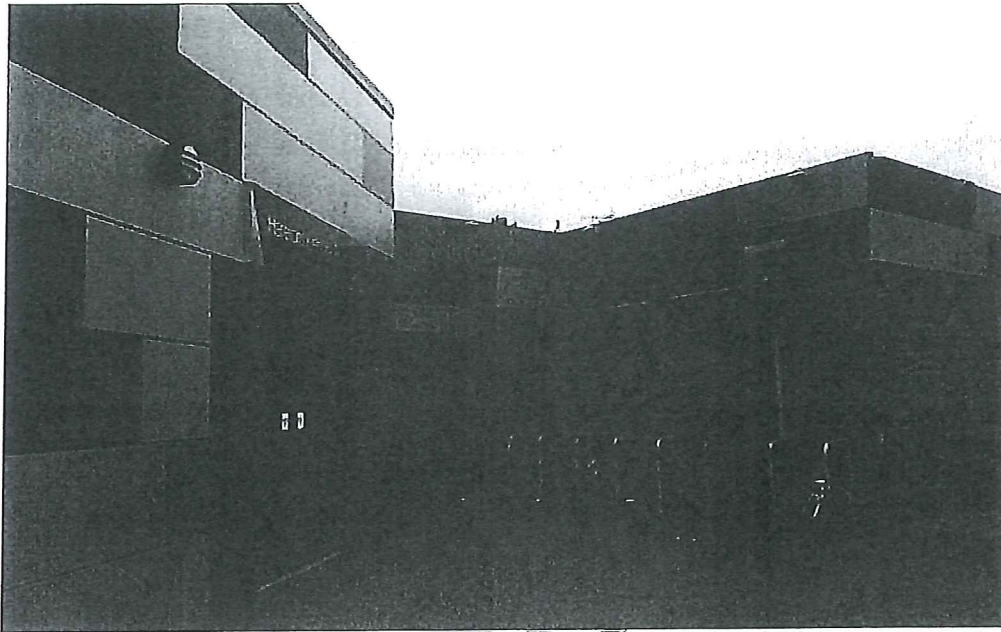


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Herefordshire Leisure Centre Valuation Strategy

Date 8th May 2017

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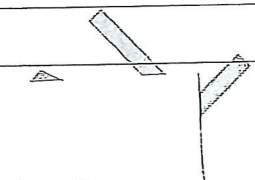
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1.0 Basis of Commission

Hub are instructed by Herefordshire Council to undertake schedules of condition for operator areas only and provide advice on valuation strategy and lease structure for all their leisure centre sites. These sites are currently let to Halo Leisure Services under leases at peppercorn rents, with shared responsibility for their upkeep. The Council's objective is to investigate whether it is feasible to pass liability for the upkeep and running of these Centre's to Halo under a full repairing and insuring lease at a commercial rent.

2.0 Executive Summary

It is considered feasible for the Council to grant a long term lease to Halo for say fifty years at an initial base rent of £x pa with a mechanism to increase this rent each rent review based upon the net surplus/turnover of the business. The lease would be on full repairing and insuring terms.

Hub recommend a financial review takes place after year five to ascertain whether Halo are on track to achieve their ten year operating model, and to review whether the model is still appropriate in the marketplace. It must be remembered that Halo has to facilitate the £9M loan repayment to the Council for refurbishment works to a number of the leisure centres.

It is Hub's opinion that the setting of an agreed open market rent of £x pa is not workable here. It is important to understand leisure centre's are not the same valuation model or market place as traditional commercial property such as Offices, Industrial etc. This is a specialist area with no comparable market evidence, usually valued under the profits test or depreciated replacement basis. Hub recommend

considering the model used for the lease for Herefordshire Racecourse and New Livestock Market.

If the decision is taken not to proceed then Halo are still "tied" into existing leases (as detailed in the schedule on page 9) expiring in 2027. However the Council will continue to be liable for their share of repairs as evidenced in the schedules attached to the leases. The basic cost for soft repairs (decoration, floor coverings, light fittings etc) is in the region of £346k (please see section 6.0). This does not take into account "hard" (Building envelope) repairs/replacement of such things as M&E, roofs, cladding etc.

3.0 Sites

There are ten sites included in this strategy:

- Bridge Street Sports Centre Leominster
- Hereford Leisure Centre
- Hereford Leisure Pool
- Ledbury Leisure Centre
- Ledbury Swimming Pool
- Leominster Leisure Centre
- Ross Swimming Pool
- The Bromyard Centre
- Lady Hawkins Community Leisure Centre, Kington
- Wigmore Leisure Centre

Over the page is set out a schedule of facilities currently provided for each of the sites.

4.0 Schedule of Facilities

Site	Sports Hall	Gym	Exercise Studio	Squash Courts	Swimming Pool	Leisure Pool	Learner Pool	Cafe	Soft Play	Toning Suite	Creche	Tennis	Indoor tennis	Sauna	All weather pitch	Golf	Outdoor pitch	Car Park	Athletic Track	Indoor bowls
Hereford Leisure Pool		√	√		√	√	√	√			√									
Hereford Leisure Centre	√	√	√	√				√	√	√					√	√	√	√	√	
Ross on Wye Swimming Pool		√	√		√									√						
Ledbury Swimming Pool		√	√		√									√						
Ledbury Leisure Centre	√		√												√					
Bromyard Leisure Centre	√	√	√																	
Leominster Leisure Centre	√	√	√		√		√	√	√									√		
Bridge Street Sports Centre												√	√		√					√
Lady Hawkins Leisure Centre	√	√	√												√					
Wigmore Leisure Centre	√	√																		

5.0 Current Lease Summary

Hub has been instructed to only comment on the centres listed below. The Council has let these leisure centres to Halo Leisure under separate leases for a term as summarised below. These are on internal repairing and insuring basis only. There are clear schedules within the leases outlining each party's responsibility in terms of repair. Essentially the Council is responsible for the building envelope/structure/fabric and all plant and machinery. Halo is responsible for internal repairs and decoration excluding plant & machinery, swimming pools etc. Please see summary schedule below.

SITE	TERM	REPAIR	RENT	ALIENATION
Hereford Leisure Pool	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Hereford Leisure Centre *	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Ross on Wye Swimming Pool *	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Ledbury Swimming Pool *	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Bromyard Leisure	25 years from	internal	£1 p/a	none save for licensing to

Centre	01/04/2002 linked to management agreement	repair only detail as per schedule		concessionaires/group companies
Leominster Leisure Centre	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Bridge Street Sports Centre	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Leominster Swimming Pool *	25 years from 01/04/2002 linked to management agreement	internal repair only detail as per schedule	£1 p/a	none save for licensing to concessionaires/group companies
Leominster and Hereford Leisure Centre Car Park	1 year from 1st august 2015	FRI	£1	None

6.0 Schedules of Condition Summary

As part of this review strategy our surveyors have undertaken and completed a schedule of condition for each of the leisure sites, with the exception of Ledbury Leisure Pool that is currently closed. The surveys were completed between August and September 2016. The schedule of condition's have been produced to outline and agree the state of a property and any potential repair work which might be needed, at the outset of any new letting agreement. These schedules are not intended to be used for any forward maintenance plans or programme of required improvements to the sites but to provide the basis of agreed condition of the property at a point in time.

The items identified in the schedules therefore relate to general wear and tear to the property and any related costings to bring the facility back to an acceptable standard and appearance.

We have summarised each site and the estimated costs pertaining to the damage and defects noted in respect of the schedule of condition parameters. Major structural, fabric, M&E repairs or replacement were captured in the figures taken from the 2010 condition surveys prepared by the Council and Hub have adapted these to give a very high level estimate for today.

Location	2016 Schedule of Condition Estimated	Estimated Total from Condition Survey 2010 (provided by HC)	High Level Condition Surveys Estimate 2016
Bridge Street Sports Centre Leominster			
Hereford Leisure Centre			
Hereford Leisure Pool			
Ledbury Leisure Centre			
Ledbury Swimming Pool (not surveyed)			
Wigmore Leisure Centre			
Leominster Leisure Centre			
Ross Swimming Pool			
The Bromyard Centre			
Lady Hawkins Community Leisure Centre Kington			
Totals			

7.0 Condition Surveys Summary

Following the advice given to the Council, in the first issue of this report (31st October 2016), Hub were then instructed to undertake full condition surveys of each leisure centre to provide a five year maintenance plan for each site. These inspections took place between February & April 2017. It was found that a vast amount of investment has occurred since the 2010 reports. The majority of those figures were attributable to Mechanical & Electrical items which have been subsequently renewed or improved during the last seven years. Halo have, and are continuing to implement a maintenance programme, including refurbishment and upgrading of each facility. Below is a five year maintenance cost summary of each centre as surveyed.

Hereford Leisure Pool	
Building	
Mechanical	
Electrical	
Building	
Mechanical	
Electrical	
Building	
Mechanical	
Electrical	
Building	
Mechanical	
Electrical	

Bromyard	
Building	
Mechanical	
Electrical	

Ledbury Leisure	
Building	
Mechanical	
Electrical	

Leominster Leisure	
Building	
Mechanical	
Electrical	

Lady Hawkins	
Building	
Mechanical	
Electrical	

Wigmore	
Building	
Mechanical	
Electrical	

All Leisure Centres - Combined	
Building	
Mechanical	
Electrical	

8.0 Proposed Strategy

The proposal is an unusual one in the market place, in that no real precedent has been set elsewhere in the country for Council owned leisure centres to be leased on full commercial terms to include a commercial market rent. The majority of local authorities have formed a trust or partnership that then runs them on their behalf with the Council contributing heavily to maintenance of the buildings. There are very few centres that do not run at a loss. We have sought opinion from other leisure consultants and it is their view this loss is at 10-15% approximately. This is due to a variety of reasons such as, location, type and age of building, maintenance of the asset, demographics, membership numbers, concessions etc. The public perception is that their local authority should be providing leisure facilities in line with healthy living promotion and their obligations to the wider community; however it is not a legal requirement.

It is essential that any proposal sits within the Council's procurement rules for "Light Touch". Hub are informed by the Council that by surrendering and renewing leases to Halo this will not contravene procurement rules, and hinder competition in the market place. Hub recommends that the Council obtains legal advice as to the true position in order to satisfy themselves that they are acting within the rules.

Any future strategy needs to take into account the Council's reputation for providing services is not put at risk by entering into a "commercial" lease; that the Council is to allow Halo to diversify and meet market trends for leisure at any given time, and has ensured that Halo keeps a commitment to the community, including continuing to provide both lower income local residents and schools/community groups access to facilities. The lease could be restricted to D1 leisure use rather than they must specifically run the sites for the public. This provides a clear use class parameter for the sites and avoids any restricted use. However they cannot at the same time price the public out. They have to remember the purpose of any agreement; this is not a lease to an established leisure operator such as David Lloyd or Virgin Active. Sport England will also need to be consulted and consent obtained to any new leases granted on commercial terms.

It should be clearly recognised that the granting of a lease for these leisure centres is not the same as the granting of a lease for an industrial unit; office or retail unit where

an established commercial market sets the rental tone for that area/location, where the occupier will be a "for profits" business.

Halo's strategy favours a long lease, indeed a virtual freehold of 99 years or longer, to enable them to have assets for purpose of raising finance for investment. Whilst the Council would still hold the freehold and receive a ground rent, following a capital receipt, it will not have control or receive any further income.

This could contravene the "light touch" approach in procurement. We would recommend that this is reviewed by a legal representative of the Council.

Hub believe a long term lease with periodic rent reviews on an upward only structure would provide the best of both worlds. Halo would be able to borrow against the asset; the Council would receive a market rental stream. The lease would be on a full repairing and insuring basis. The Council recognises that whilst some major refurbishment works have been undertaken, a number of sites require attention, an obligation which would now pass to Halo. They currently have to service the repayment of a £9M "loan" facility from the Council and it is essential that this is met in full and on time.

Based on the Racecourse and the requirements of the Council and Halo it may be possible to set a nominal rent of say _____ for all eleven sites under a single lease, which equates to less than _____. This would be the base rent, set for the first five years. At the first rent review you would reassess as mentioned above the trading model and review the whole financial elements related to the lease. If there is a positive net surplus then a weighting/mechanism would be applied to the base rent to allow for a rental increase at each subsequent rent review. The

mechanism, if adopted, should to be agreed between the parties as part of the lease negotiations.

9.0 Next Steps

Hub recommends that the Council reviews this report with a Council legal representative.

The Council needs to understand their potential obligations under the current lease for their repair responsibility.

If the Council decided to issue a surrender and re-grant in line with this strategy then the full condition surveys will allow the Council to monitor a planned maintenance programme that Halo would be obliged to undertake over the following five to ten years which will clearly assist decisions/negotiations on rent, when reviewing Halo's financial model at years five and ten.

A meeting should be arranged with Halo to talk through this proposal and establish what Halo's aspirations are.

It must be noted that this report sets out the mechanism but both parties would need to employ professional advisors to negotiate a clear mutually agreeable set of heads of terms.

The Property & Design Consultants

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