Agenda item No. 8

Bristol City Council
Business Change and Resources Scrutiny Commission
15 September 2014

Report of: Mike Allen – Finance Business Partner

Title: Bristol Arena Funding **Ward:** Citywide

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Recommendation

That the Commission consider the proposed funding arrangements for the Bristol Arena Project.

Summary

The Council approved £90m funding for the Bristol Arena as part of the Capital Programme. A number of funding streams have been identified to pay for the construction of the Arena and in cash terms, our current model suggests that the Arena will break even over 25 years.

Introduction

Bristol Arena was included in the Capital Programme at a cost of approximately £90m (Appendix A). £90m pays for the base build of the Arena in a "horseshoe" configuration, on the Diesel Depot site south of Bristol Temple Meads Station. It does not include the cost of purchasing the site from the HCA.

Costs included are construction, contingency, fees, inflation, council costs and limited on and off site works. Building a new arena usually requires a measure of public funding as the rentals provided by an operator running an arena would be insufficient to cover the cost of borrowing for its construction. This is demonstrated by a number of recent UK and European arena projects including Leeds, Manchester and Copenhagen, each of which have required an injection of public money.

The main exception would be arenas where there is a high level professional sports team as the anchor tenant. However, this was not considered to be a viable option for Bristol and didn't fit in with the aim of providing a multi-use, cultural venue.

Background

The decision to build the Bristol Arena was confirmed by its inclusion in the Capital Programme approved by Full Council on 18th February 2014 as part of the BCC Capital Investment Programme. At that time the funding options to cover the cost of an arena were being explored with the aim of providing as near a cost neutral solution for Bristol City Council as possible.

The Council received an Outline Business Case (OBC), dated November 2013, setting out the case for Bristol Arena and providing a financial commentary detailing potential funding sources to cover the cost of an arena build.

As of September 2014, the search for an arena operator is in progress. One of the key selection criteria will be the financial evaluation. This is based on the rental that an operator would pay to run Bristol Arena, plus any capital savings or capital contributions proposed. It is expected that the selected operator would have a contract and lease to run the Arena for at least 25 years and that rentals would be indexed annually.

In addition to operator rentals, the council is expecting to get income from the Economic Development Fund, part of the City Deal, which is to be signed between Bristol City Council, North Somerset Council, BANES and South Gloucestershire Council. The final application for funds for Bristol Arena is being submitted during September 2014.

Outline Business Case (OBC) assumptions
The OBC written by the council's advisors set out the cost of developing Bristol Arena. The development cost was based upon a benchmarking of recent arena builds in the UK and Europe which provided the council with the best cost information available for decision making.

In addition to providing cost estimates, the OBC provided ideas for funding. The funding sources noted for consideration were:

- Arena rental payments (from the operator)
- Car parking income
- Retained business rates from the TQEZ (City Deal)
- "Other income" (not specified)
- Alternative sources of income such as grants
- Sale of assets

The council asked that the potential for car parking income to be reviewed in the OBC given the success of that source of income for the new Leeds Arena.

Funding the Arena – assumptions and terminology
A number of funding streams will be discussed below. It is important to have clarity over what is being described. The key assumption is that the council will fund the construction of the arena. For the purposes of reporting, the following modelling assumptions are made:

- The council will borrow the full amount required to building the Arena
- All borrowing will be from PWLB (public works loans board)
- Repayment costs are based on annuity loans (equal annual payments)
- Income received (such as rentals from an operator) are "capitalised", i.e. calculating the value of an annuity loan that the income would support (see below).

The aim of using such assumptions is to allow the comparison of financial offers from bidders and to provide a methodology to allow consistent reporting of arena finances to the council.

Any financial position will be "notional" as the cost to the council will vary due to the impact of treasury management strategies. For example, the council may decide to borrow ahead of requirements, if this provides additional value, or decide to use cash balances or reserves instead of borrowing if that provides better value. Interest rates will change over time.

Capitalisation of income assumptions
At present, (4 September 2014) using the current PWLB borrowing rates, it costs £61,986 a year to borrow £1m over 25 years. This means to capitalise any income stream, the income should be multiplied by 16.13, which is the result of dividing £1m by £61,986.

Funding the Arena –assumptions from OBC
The main reports received by Cabinet were in December 2013 and January 2014.

Cabinet 5 December 2013
This report dealt with the operator model that the council wished to use and also provided an outline of the proposed arena funding package, based on the assumptions from the OBC and a specific car parking report commissioned from ARUP. It was reported that the combination of income from car parking and from operator income would leave a funding (capital) gap of £53m which would be covered by income from City Deal.

The main financial comments concentrated on the how the Council might receive income from City Deal. In particular, the impact should City Deal money income build up over time, rather than being 100% available from the start of the project.

The reason for this analysis was that the precise mechanics of City Deal were in their infancy and it appeared prudent to set out the cost to the council of a range of potential income scenarios. Some limited analysis was provided regarding the impact of variations in car parking and operator revenue income streams.

The conclusion was that if City Deal funds were available, then there should be no recurring annual revenue implications for the council.

Cabinet 16 January 2014
The background section of the report covered the same financial issues as for December Cabinet and noted that car parking income, Arena rentals and City Deal should cover the Arena costs.

The detailed report provided a commentary on financial risk, noting that City Deal may not provide income to match the cost of prudential borrowing from day one and that car park income may vary year on year.

Funding the Arena – updated assumptions

The potential income streams identified for the Arena now include:

- Car parking income
- EDF/ City Deal
- Operator Rentals

a) Car parking income

The OBC identified car parking as a viable income stream for the council. A report by ARUP in 2013 suggested that the council might be able to capture 60% of car parking visits associated with the arena each year and that this could result in net income of around £250,000 to £300,000 per annum plus the potential for £1.2m from day time users.

This income would be facilitated by offering arena customers a car parking option as part of their ticket deal. The report recommended a 1,000 space car park should be available within a short walk of the arena.

The ARUP report identified two potential sites near the proposed arena, one which supported the provision of an “at grade” (surface) car park and one that supported a multi-story car park. An important rationale for these sites was that income could be generated in the evenings and weekends from arena related parking and during the day, income could be generated from commuters in the TQEZ.

The multi-story option was discounted as a cost of construction of £15m was too high, when combined with a site purchase, to enable a surplus to be generated. The surface car park was recommended as its construction cost of £2.7m could with both evening and day time use, generate a surplus. The ARUP report did not take account of the cost of acquiring a site to build a car park. Nor did it include unforeseen costs such as pedestrian access from the car park to the arena, which on a subsequent, more detailed review, potentially raised capital costs by at least £3m, due to some complex property issues.

Once access and site purchase were factored in, the total capital cost of a surface car park was estimated to rise to between £9m and £16m. This was only potentially viable with day time use. Day time use is against current planning policy and the most recent review of an access route from TQEZ to the car park, for day time users, suggested the income targets in the report were unlikely to be achieved because of poor access.

We are currently reviewing car parking options for the arena project within the context of the needs of the TQEZ.

b) EDF/City Deal

City Deal is a business rates retention arrangement. It is being administered by the West of England LEP. The current bid from Bristol City Council is for funding to support £53m of borrowing. We would expect that the allocation of funds from City Deal would cover all the associated borrowing costs of a £53m loan. The main risk is that the income is reliant upon economic growth in enterprise areas and zones. However, prudent modelling has been undertaken to ensure that growth forecasts are as robust as possible and the council expects that the income predicted for the arena will be realised.

c) Operator Rentals

Operator rentals are currently the subject of a procurement exercise and so the table below shows funding based on early estimates of operator rentals.

Financial position

The Bristol Arena build is estimated to cost approximately £90m. The cost of FF&E (interior fit out) will either be funded directly by the successful operator or included in additional rental payments. This is expected to total approximately £3m. Of the remaining £87m to fund, £53m is expected to come from City Deal and the remainder from operator rentals and other council resources and income generating options.

The funding assumptions, at OBC and now, are set out in the table below.

Funding £m*	**OBC - Autumn 2013**	**September 2014**
Car park income	10m	0m
City Deal	53m	53m
Operator rentals	**24m	**25m
Other	0m	0m
FF&E (internal fit out)	3m	3m
Total	90m	81m
Capitalised funding gap	0m	9m

* Expressed as capitalised income streams
** Increase due to falling interest rates

Funding gap
The funding gap identified above at £9m would translate into a first year cost of around £550k. This is based on the assumptions for income in the table above and a PWLB interest rate as at 4 September 2014. This is only a snap shot as the overall financial situation for the arena would vary over time and with the bids received by potential operators.
Taking into account the following assumptions:

- City Deal covers the cost of £53m of PWLB borrowing
- Operator rentals are indexed at 2.5%, and
- FF&E is at no net cost to the Council

Our current modelling suggests (using the data set out in this report) that the arena would be have a reducing cash flow deficit from year 1 to year 13. After year 13, the model suggests that the arena would be in annual surplus and should deliver a break even position around the end of year 25 of operation.

This is without taking into account a number of other avenues being currently explored for income generation or any of the wider economic benefits that building an arena in Bristol should being to both the council and the local economy.

Risk

FIGURE 1 The risks associated with current funding assumptions						
RISK Threat to achievement of the key objectives of the report	INHERENT RISK (Before controls)		RISK CONTROL MEASURES Mitigation (ie controls) and Evaluation (ie effectiveness of mitigation).	CURRENT RISK (After controls)		RISK OWNER
	Impact	Probability		Impact	Proba-	
Operator rentals are lower than forecast	**High**	**Medium**	BCC have engaged expert advisors to .provide estimates of Operator rentals. We are assured that the estimates are conservative.	**Medium**	**Low**	Project Board
PWLB interests rates increase and increase the cost of loans	**Medium**	**Medium**	Treasury management advises that significant rate increases will be signposted and BCC has the option to borrow ahead of need	**Medium**	**Low**	Project Board
City Deal provides less support than predicted	**Medium**	**Medium**	BCC are fully engaged in the process of estimating City Deal and its capacity to provide estimated payments to Councils	**Medium**	**Low**	Project Board
Inflation increases Arena build costs	**Medium**	**Medium**	BCC have expert advisors on Arena costs who will provide warnings if contingencies are not sufficient	**Medium**	**Low**	Project Board

Consultation and scrutiny input:

a. Internal consultation:
Strategic Directors, Service Directors and the finance team.

b. External consultation:
Not applicable

Other options considered:
No other options are considered prudent at the present time.

Public sector equality duties:
There are no proposals in this report which require either a statement as to the relevance of public sector equality duties or an Equalities Impact Assessment.

Environmental checklist / eco impact assessment
Not applicable.

Resource and legal implications:

Finance

a. Financial (revenue) implications – Service Director - Finance:

As set out in the Report.

b. Financial (capital) implications:
As set out within the report.

c. Legal implications:
Not applicable for this report

d. Land / property implications:
Not required for this report

e. Human resources implications:
Not applicable for this report

Appendices:

Appendix A – Estimated Arena Development Costs

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Arena development costs (AECOM)	**£**
Base Cost	55,072,000
Fees at 15%	8,261,000
FF&E at 5%	3,167,000
Development contingency at 10%	6,650,000
Inflation from 8/14 to 11/15 at 9.71%	7,100.000
Sub total	**80,250,000**
Externals and abnormals	8,110,000
Total Cost	**88,360,000**
BCC development costs	1,800,000
Estimated interest during construction	250,000
Grand total	**90,410,000**