

CABINET MEETING: 26 NOVEMBER 2020

INDOOR ARENA PROCUREMENT

**INVESTMENT & DEVELOPMENT
(COUNCILLOR RUSSELL GOODWAY)**

AGENDA ITEM: 1

Appendices 1 – 15 of this report are not for publication as they contain exempt information of the description contained in paragraphs 14 and 16 of part 4 and paragraph 21 of part 5 of Schedule 12A of the Local Government Act 1972.

Reason for this Report

1. To provide Cabinet with an update on the procurement process to secure a private sector partner to deliver and operate a new Indoor Arena at Atlantic Wharf, Cardiff Bay.
2. To seek Cabinet authority to:
 - (a) Appoint the ‘Preferred Bidder’ developer/operator consortium and enter into the “Preferred Bidder stage” of the competition as provided for in the procurement process;
 - (b) Authorise the Council to enter into the final Full Business Case stage including a Pre-Contract Services Agreement (“PCSA”) with the Preferred Bidder;
 - (c) Progress the land strategy to enable delivery of the Arena and the wider masterplan;
3. To outline a number of obligations that will be placed on the Council to support delivery of the new Indoor Arena following completion of the Full Business Case.

Background

4. The new Indoor Arena project supports a number of Council commitments, priorities and strategies including:
 - Attracting more visitors to the city that stay longer
 - Supporting growth in the local economy and creating jobs
 - Supporting the next phase regeneration of Cardiff Bay
 - Eliminating poverty and promoting equality
 - Promoting culture and creativity
 - Supporting the Cardiff Music Strategy

5. Delivering a new Indoor Arena is widely regarded as the missing piece of city infrastructure needed to cement Cardiff's international reputation as a major events city. It has been a long-standing ambition going back as far as the Cardiff EU Summit in 1999 and is an aspiration shared by successive Council administrations who have retained a ring-fenced budget since 2006.
6. The city's business community have also promoted the project over many years, particularly the hospitality sector. Their support was recently re-affirmed through the consultation process for the Council's new Economic Strategy launched in April 2019.
7. The transformation of the city's economy from heavy industries to knowledge-based economy has involved projecting an image of the city as a clean, safe and vibrant place to live, work and visit. As part of this, and for over 3 decades now, Cardiff has progressed a strategy to attract visitors to the city from outside of the local area, including international visitors. Significant investment has taken place in city infrastructure that has made Cardiff an attractive place to visit such as the St David's 2 Shopping Centre and the Principality Stadium in Cardiff city centre, and the barrage and Wales Millennium Centre in Cardiff Bay. Hosting major events in the city has also been a central part of this strategy, and Cardiff has been successful in competing for events at the very highest level.
8. The strategy of attracting visitors to the city remains a key economic priority today. The Council's strategic policy documents Capital Ambition and the Corporate Plan outline commitments to attract 'more visitors that stay longer' and to closing the gap with neighbouring cities such as Bristol. Cardiff attracts over 20m visits per annum, which compares well with most UK cities. However, just short of 400,000 of these visits are from outside of the city-region. Bristol achieves more than 50% more visits from outside of their local area; Liverpool more than double Cardiff; and Edinburgh over 2.2m.
9. The new Indoor Arena will help Cardiff attract more visitors from outside the city-region. A bigger capacity arena in itself will accommodate more fans and therefore should at the very least deliver a proportionate increase in the number of external visitors. The step-up in capacity will lead to a step-up in the quality of acts attracted to play at the new venue, and a step-up up in the quality of facilities available to fans such as hospitality areas and VIP experiences, that should generate much more than a proportionate increase in outside visitors. More outside visitors will increase on-site turnover, as they tend to spend more, but the greater impact will be realised through increased spend across the wider local economy.
10. A report commissioned by the operators of the Motorpoint Arena in 2015 estimated the local economic impact of the venue to be circa £30m per annum. The Motorpoint Arena is a 5000 seat/7500 capacity venue that hosts circa 130 events per annum attracting circa 450,000 visits per annum, supporting around 500 full time equivalent (FTE) jobs. The estimated £30m economic impact was based on circa £14m of spend on-site and the rest spent in the wider local economy. The analysis was based on a typical local resident spending in the region of £30-£45 per visit (in 2015) compared to

circa £300 for visitors that stay in the city overnight. The report estimates that in 2015, circa 27% of the audience came from outside of the local area, and circa half of these stayed overnight.

11. In comparison, major new arenas in cities like Glasgow and Liverpool are delivering a different level of impact on their local economies. The Glasgow Hydro complex, which includes an adjacent exhibition centre and conference centre has a capacity of 12,500. In 2019, the venue hosted 205 events, attracting 1.82m visitors, delivering an estimated economic benefit of £354m and supporting around 5,000 jobs. The Liverpool M&S Bank Arena also has an adjacent conference centre as part of its complex and has a capacity of 12,000. In 2019, the venue hosted 200 events, attracting over 1m visitors, delivering an estimated economic benefit of £221m, and supporting over 1,500 jobs.
12. The proposed new Indoor Arena in Cardiff will meet the Council's minimum capacity requirement of 15,000. Further detail is provided in Confidential Appendix 1.
13. The location of the new Indoor Arena in Cardiff Bay is also of strategic importance to the Council, both in terms of the Corporate Plan commitment '*to write the next chapter in the regeneration story of Cardiff Bay*' and the major corporate priority to tackle poverty and improve equality and opportunity for the residents located in the 'Southern Arc'.
14. The Atlantic Wharf regeneration scheme, anchored by the new Indoor Arena, is one of two key strategic economic commitments set out by the political administration in their strategic policy vision document Capital Ambition. The area has been transformed over recent decades, but there remains significant work to do to establish Cardiff Bay as a *premier UK visitor destination*.
15. The new Indoor Arena is the primary catalyst for the regeneration of Atlantic Wharf, and the Atlantic Wharf project is the primary catalyst for the next phase regeneration of Cardiff Bay. The Atlantic Wharf scheme will deliver a major extension to Cardiff Bay's Inner Harbour of similar scale and impact to the St David's 2 development in Cardiff city centre. In doing so it will provide a long-term sustainable footing for the businesses that have already invested in the area, as well providing the necessary footfall uplift to attract the next phase of new investment. It will also directly support the Council priority to *improve the link between the city-centre and Cardiff Bay* by transforming the southern end of Lloyd George Avenue, and by supporting the delivery of new public transport infrastructure and active travel links along the route.
16. The new Arena will be located in the Butetown ward in the Southern Arc, which covers around two fifths of Cardiff. If considered as a discrete area in its own right, the Southern Arc would be by far the most deprived area in Wales, as defined by the Wales Index of Multiple Deprivation. The Butetown ward has for some time experienced poorer economic outcomes than the Cardiff and Welsh averages, and current claimant count data suggests that the unemployment rate for the area is 2.4 times higher than both the Welsh

and UK average. The BTN01 Lower Super Output Area within the Butetown Ward is also amongst the most deprived in Wales according to the 2019 Wales Index of Multiple Deprivation and ranked in the worst 10% of performing areas in terms of both the Overall Index as well as the income, health, housing and physical environment domains. The new Indoor Arena is located on the boundary of BTN01, with some of the site in BTN01.

17. The Arena project will provide a substantial number of new jobs in its own right, both through the construction phase, and through its long-term operation. The Arena will be located in close proximity to many of Cardiff's most disadvantaged communities. Through the procurement process to appoint an operator/developer consortium to deliver the new Indoor Arena, the Council has secured a number of local community benefits (see Confidential Appendix 1).
18. In October 2019, Cabinet authorised a new Music City Strategy, to promote Cardiff for grassroots music. Internationally renowned advisors Sound Diplomacy developed the strategy through collaboration with the local sector and commented that *"the new Arena will attract more International acts to Cardiff and have a positive impact at all levels of the live music ecosystem, from the grassroots venues to our major spaces."* In their study, Sound Diplomacy set out that the Arena development will become a fundamental component of Cardiff's 'Music City' brand. It will plug the gap of venue size so any and all acts have a stage in the city and will support the development of a home-grown industry, e.g. event related production staff. Sound Diplomacy suggest that the new Indoor Arena will have a place-making impact by supporting the clustering of performance and production capacity in the Cardiff Bay area.
19. Although the aspiration to deliver a new Indoor Arena has been around for some time, the project has taken a major step forward in the last few years. In February 2018, Cabinet authorised the selection of Atlantic Wharf as the preferred location for delivery of a new Indoor Arena.
20. In February 2019, as part of the budget setting process, Cabinet approved an affordability envelope in the Council's Medium Term Financial Plan to support delivery of the new Indoor Arena including financial provision for the acquisition of the Red Dragon Centre site.
21. In July 2019, Cabinet gave authority to begin a procurement process to secure a developer/operator consortium to deliver an Indoor Arena at Atlantic Wharf, Cardiff Bay with a minimum capacity of 15,000.
22. In December 2019, Cabinet approved the acquisition of the Red Dragon Centre investment and other land. The timing of this acquisition was significant as it provided bidders in the procurement process with a clear signal of the Council's commitment to the project in advance of the final stages of the procurement process, which required the bidders to make a significant investment to prepare their final bids.

Procurement Process

23. The Council has embarked on a procurement process that is similar to the Competitive Dialogue procedure (as more particularly described in the Public Contracts Regulations 2015 (as amended). However, as the procurement falls under the scope of the Concession Contracts Regulations 2016 (CCR) the Council is not bound by the formalities or rules governing the Competitive Dialogue procedure. This in turn, has enabled the Council to utilise greater flexibilities in the conduct of the competition.
24. An EU public procurement exercise was commenced by the Council on 20 August 2019 by issuing a Concession Notice in the Official Journal of the European Union (“OJEU”).
25. A brief overview of the stages of the procurement process is set out below:

Pre-qualification Stage

- The initial stage of the procurement process involved the Council inviting bidders to express their interest by way of completion and submission of Selection Questionnaires (“SQ”).
- Eight SQ applications were received from the market prior to the deadline and following an evaluation process two bidders were successfully taken through to the tender stages of the competition.

Invitation to Submit Outline Solutions

- The Invitation to Submit Outline Solutions (“ISOS”) stage was the first stage of dialogue with the two bidders who were successfully shortlisted at the SQ stage.
- At the conclusion of the ISOS stage, bidders were required to submit their Outline Solutions which the Council did not formally review but considered their contents to ensure that bids were sufficiently on track towards being developed and submitted as Final Tenders later in the process.
- Upon reviewing and being satisfied with the progress of the Outline Solutions both bidders were invited to continue in dialogue with the Council via the issue of the Invitation to Continue Dialogue (“ITCD”) document in March 2020.

Invitation to Continue Dialogue

- This stage involved the Council entering into further dialogue with bidders to align the content of their bids with the Council’s strategic goals. In addition, the Council received reassurances from bidders that the project could be delivered within the stipulated affordability envelope, which was a key objective for the Council.

- Dialogue continued with bidders over a number of weeks until the Council deemed it was satisfied that sufficient progress had been made with bid solutions.
- During this further dialogue stage, the impact and disruption that the COVID-19 outbreak would cause was being realised. As a result, delegated approval was provided by Cabinet to refine the award criteria and weightings to allow the Council to assess bidders' ability to deliver the project despite the disruption caused by the pandemic.
- Once authority had been granted the dialogue stage was brought to a close by issuing the Call for Final Tenders document to bidders.

Call for Final Tenders

- The CFT stage is the final tender submission of the procurement process. It confirms the evaluation criteria, weightings and methodology that would be used to assess Final Tenders.
- This document was issued to bidders on 17 July 2020 with a Final Tender deadline of 12 noon on 18 August 2020.
- The Council can confirm that Final Tenders were received from both bidders prior to the expiry of the above deadline.
- Final Tenders have now been evaluated and ranked to determine the most economically advantageous tender which the Council is now seeking approval from Cabinet to appoint as the Preferred Bidder.

Preferred Bidder Stage

- The Preferred Bidder stage is another stage of the procurement process and does not constitute a contract award decision signalling the conclusion of the competition.
- The Preferred Bidder stage will allow the Council to work with the Preferred Bidder to finalise the contractual arrangements and work up its design to deliver the Arena and the Travelodge Hotel.
- The Preferred Bidder stage will be governed by a PCSA that the Council will enter into with the Preferred Bidder. Cabinet approval is therefore sought to enter into the PCSA as set out in Confidential Appendix 1.
- The overall process has been managed by the Council in consultation with an external professional team to audit the legal and technical elements of the project to ensure a robust consideration of the procurement and the final tender submissions, as set out in Confidential Appendix 1.

Preferred Bid

26. The procurement process has now reached the stage where the Council has received Final Tenders from the two bidders who participated in the competition in relation to the delivery of an Indoor Arena and Travelodge Hotel within the Council's affordability envelope.
27. Through an evaluation process the Council has identified a Preferred Bidder that provides the most economically advantageous tender, which the Council is minded to appoint.
28. The Preferred Bid will deliver an Indoor Arena which meets the minimum capacity requirement of 15,000 as specified by the Council. Financial details of the Preferred Bid are set out in Confidential Appendix 1. In summary, the Preferred Bidder has agreed to enter into a long-term lease arrangement, supported by a Parent Company Guarantee that will be used to forward fund the development costs. In order to maximise the value of the lease, the Council will be required to provide a form of rental guarantee over the lease. There is also a requirement for the Council to provide a capital contribution, which amounts to less than 15% of the total cost of delivery. The amount set out in Confidential Appendix 1 is a maximum contribution which could be reduced if the cost of borrowing reduces between now and when the Council enters into a Development Agreement. The Bid sits within the financial envelope set by the Council at the start of the procurement process.
29. Cabinet is now required to approve the appointment of the Preferred Bidder. The next stage will be to undertake a Full Business Case appraisal to agree final designs and costs before entering into a Development Agreement in the summer 2021. Further legal advice is set out in Confidential Appendix 15.

Issues

Pre-Contract Service Agreement ("PCSA")

30. Given the extent of work involved in the Full Business Case appraisal, the Council will be required to provide the Preferred Bidder with a level of comfort to spend a significant amount of money before having the commercial security of a Development Agreement. This will be achieved through a PCSA. The Full Business Case appraisal will involve developing the detailed design to RIBA Stage 4 i.e. to the point where plans are ready to be submitted for planning permission and normally circa 5% of the total project budget is allocated towards these costs. Further site surveys and due diligence will also be required to confirm the detailed cost plan and to ensure the project remains deliverable and within the Council's affordability envelope.
31. Entering into the PCSA will require the Council to underwrite the Preferred Bidder's costs in certain circumstances (up to a pre-agreed cap) as set out in Confidential Appendix 2. If on completion of the Full Business Case the Council decides not to proceed with the development, the Council would then become liable to pay for these costs (as set out in Confidential Appendix 1). If, on the other hand, the developer fails to develop the scheme

within the affordability envelope and the scheme does not progress, the developer would remain liable for those costs. If the project proceeds as expected, the costs will be absorbed within the overall cost of delivering the Arena development.

32. If the Full Business Case is approved and the development progresses, a number of obligations will be placed on the Council in the Development Agreement. These obligations are set out in the 'Conditions Precedent' document set out at Confidential Appendix 1.

Conditions Precedent - Land Strategy

33. There is a requirement for further land assembly to be undertaken by the Council that is required to be completed by the time the Full Business Case is approved to enable the project to progress seamlessly into a Development Agreement. The land strategy is set out in Confidential Appendix 3 including an overview of current negotiations and the risks and consideration required to progress these matters.

Conditions Precedent - Car Parking

34. An important component of the 'Conditions Precedent' commitments will be an obligation placed on the Council to retain the existing car parking provision at Atlantic Wharf, with a minimum of 1,500 car parking spaces being available no later than the time of opening of the new Arena, subject to planning. A number of options have been considered for the location of this car-parking provision, as set out in Confidential Appendix 4, along with the Council's preferred solution.
35. The transport strategy submitted as part of the planning documents will be public transport and active travel led. The Preferred Bidder is also very supportive of the Council's Cross-rail proposals and believes the footfall generated by the new Arena will help to provide the fare-box contribution required to support an extension of the new Metro eastwards to the new St Mellons Parkway station and west to Cardiff Central.

Conditions Precedent - Associated British Ports (ABP) Covenant

36. As part of the Land Strategy the Council has worked with ABP to understand various site constraints including a restrictive covenant over the use of the County Hall site as set out at Confidential Appendix 1. The Council has agreed Heads of Terms with ABP to remove the restrictive covenant, permit the Arena to be built adjacent to the dock feeder and to provide technical advice relating to a number of site constraints including the re-alignment of the dock feeder as set out at Confidential Appendix 5. Independent valuation advice is attached at Confidential Appendix 6.

Conditions Precedent - Travelodge Hotel

37. In January 2020, the Council purchased the Red Dragon Centre as an investment and to provide the opportunity for the Council to assist in the delivery of the new Indoor Arena through the regeneration of the site. The

existing Travelodge hotel lease formed part of this investment. The hotel was in the process of being extended to provide additional bedroom capacity following the granting of planning permission. In order to accommodate early delivery of the new Indoor Arena, the preferred location for the Travelodge hotel is at the rear of the Arena and discussions have taken place with Travelodge to transfer their leasehold interest to a new and larger hotel in that location.

38. Unfortunately due to the pandemic, in June 2020 Travelodge proposed a Company Voluntary Arrangement (CVA) of its whole portfolio including their hotel in Cardiff Bay. The CVA has led to a pause in the rent and a stepped repayment structure to recover the rent. A new break clause has also been agreed. This in effect has been gifted to the Council in terms of having vacant possession of a site without the requirement to compensate under normal commercial terms.
39. Over the past few months, the Council has continued dialogue with Travelodge regarding a new hotel to be delivered as part of the Arena development. The aim is to complete an agreement to secure the relocation of Travelodge prior to the revised break notice date by entering into an Agreement for Lease. This agreement will be transferred to the Preferred Bidder upon signing of the Development Agreement for delivery by the Preferred Bidder as part of the Arena development. Dialogue is progressing positively with Travelodge on Head of Terms and towards an 'Agreement for Lease' as set out at Confidential Appendix 7. Independent valuation advice is provided at Confidential Appendix 8).

Heat Network

40. It has become apparent through the procurement process that the delivery of the proposed new Heat Network needs to link-in with the programme for delivery of the new Indoor Arena, to ensure both projects optimise value and costs. The bidders clearly identified financial and sustainability benefits of utilising the network. However, this is on the basis the Heat Network is delivered in conjunction with the Arena; if not, there could be significant costs and programme risks for both projects which may affect viability, as set out in Confidential Appendix 1.

Project Management Resources

41. To progress the Arena project through the next stages of development the Council will need to allocate further budgets and resources to manage the process. Confidential Appendix 2 sets out the resources that are required to ensure designs, specifications, costs and programmes meet the Council's requirements, and to ensure the development links with the various opportunities/projects that make-up the wider Atlantic Wharf regeneration.

Other Future Considerations

42. In addition to the Conditions Precedent outlined above, that will need to be complied with after entering into the Development Agreement in the summer 2021, there are a number of additional issues that will need to be considered

in the context of the wider masterplan. These include the long-term future of the County Hall building, the redevelopment of the Red Dragon Centre. In particular, choices relating to the wider regeneration of the Atlantic Wharf area will impact on service infrastructure such as energy provision, the Heat Network, the SUDs solutions and transport strategies etc.

43. Upon signing the PCSA the Preferred Bidder will be working towards submitting the Full Business Case by no later than May 2021. Assuming the successful completion of the "Preferred Bidder stage" this will require a further Cabinet approval to proceed to award the award of contract with the Preferred Bidder. The development programme attached at Confidential Appendix 1 identifies the key milestones associated with the delivery of the new Arena.

COVID-19

44. In March 2020, the COVID-19 pandemic emerged across Europe and has resulted in a full shut-down of the live entertainment industry since then.
45. Despite this, the procurement process to secure a developer/operator consortium for the new Indoor Arena in Cardiff has progressed unabated. The procurement process involved the two largest Arena operator/promoters globally who were extremely confident of the long term resilience of the sector.
46. As set out above, the Cardiff project is a private sector led proposal, supported by the Council. That means the private sector will be taking the lion's share of the risk associated with delivery of the project, in the form of a commitment to a long-term commercial lease. Furthermore, the Preferred Bidder has provided a Parent Company Guarantee which provides the Council with an additional level of security.
47. It is viewed by the industry that the COVID-19 pandemic has caused a 'pause' in the live entertainment calendar rather than a loss of business, as the vast majority of shows will still be presented once restrictions allow, likely resulting in a much more congested 2021/22 event calendar. In some countries where the pandemic is under greater control, there has already been a return of live events.
48. The competition for market share has continued during lockdown. New Arena developments have progressed in Europe and in recent weeks new arenas have been announced for Milan and for Manchester. The arenas in Gateshead and most notably in Bristol are still progressing. The Preferred Bidder's strategy is to establish the Cardiff Arena as a top tier UK Arena and the premier Arena in South West region of England and Wales.
49. The June 11 2020, '*Restart Recover Renew*' Cabinet Report noted the need to consider the opportunity for the Council to stimulate local development, and that renewal work would be led by major projects that would have the most positive impact on job creation, inward investment and the environment. In light of the need to accelerate such investment, the new Indoor Arena represents a significant 'oven ready' project of scale that would

make a sizable impact on job creation and business development. Put simply, the new Arena project represents an opportunity to lever much needed capital investment to support the renewal of the city economy.

Local Member consultation

50. Local Members are aware of the proposals and will be consulted as part of the planning process.

Scrutiny Consideration

51. The Economy & Culture Scrutiny Committee considered this item on 16 November. Any comments received will be circulated at the Cabinet meeting.

Reason for Recommendations

52. To seek authority progress to the Preferred Bidder stage of the public procurement process and to develop the Full Business Case for the delivery of the new Indoor Arena and Travelodge Hotel.

Financial Implications

53. This report, and in particular the confidential appendices, presents the outcome of the Call for Final Tenders (CFT) and is identifying a preferred bidder. This report sets out the financial commitments that the Council would need to enter into for the Indoor Arena to be delivered, the obligations that the Council must meet (Conditions Precedent), and the next steps to be taken.
54. This report reflects a significant step in the process of delivering an Indoor Arena in Atlantic Wharf and will require several decisions and financial commitments to be made in order to progress to the "Preferred Bidder stage" of the competition and enter into the PCSA with the Preferred Bidder. It should be noted though that whilst a preferred bidder may be appointed at this stage, a future Cabinet decision (expected no later than May 2021) will still be necessary before proceeding to contract award. Further due diligence is still required through the "Preferred Bidder stage" to mitigate identified risks, to confirm Indoor Arena viability and affordability for both Council and the Preferred Bidder, as well as being sure both parties can satisfy State Aid requirements. Further financial implications will therefore be provided on these more specific elements in a future cabinet report.

Council Capital Contribution

55. The procurement process has confirmed that the new Indoor Arena is able to operate commercially, without any ongoing Council subsidy, once delivered. In line with other new Arenas delivered in the UK over the last decade though, a public sector contribution will be required towards the construction costs of the Arena. The Council has previously made provision within the capital programme and medium term financial plan (MTFP) to enable a state aid compliant capital contribution to be made towards Arena

construction costs, with the scale of Council capital contribution required to be tested through the competitive procurement process up to an identified maximum cap. With final tenders now received, it has been confirmed that the scale of Council capital contribution being sought by the Preferred Bidder for construction of the Arena is below the maximum cap allowable, and substantially less than the provisions made within the Capital programme.

56. The maximum level of capital contribution required is set out within Section 3 of the Finance Report included as Confidential Appendix 2. The capital contribution is due to be funded by a mixture of capital receipts and borrowing, with the most substantial element of the Council contribution due to be funded by earmarked capital receipts. However, at this stage some of these capital receipts are yet to be realised. Any significant delays or non-realisation of these capital receipts is likely have an adverse impact on the Council's ability to meet this level of proposed gap funding contribution. See Section 5 within Confidential Appendix 2 for details of the Funding Strategy.

Income Strip / Lease and Lease Back Arrangement

57. As detailed within the report, to facilitate delivery of the Arena the Council will also be required to enter into an 'income strip/lease and lease back' arrangement with the Preferred Bidder and a funder. This is in addition to the capital contribution referred to above.
58. An income strip (lease and lease back arrangement) is a simple, tried and tested financing structure that can be utilised to generate a significant capital stack for development purposes. This structure enables the Preferred Bidder to utilise the Council's superior financial covenant strength to obtain more attractive lease and finance terms in order to make a project more financially viable, whilst importantly the freehold land and property interests are retained by the Council at all times. (See Confidential Appendix 14 for more information on income strips / lease and lease backs, how they work and the advantages and risks of entering into such an arrangement).
59. By utilising this funding solution the Council will be entering into a long-term 45 year obligation at financial close to pay an indexed linked rental to a financial institution in exchange for an upfront capital sum (to be used for Arena construction). The Council's lease obligation will be offset by entering into a back-to-back lease arrangement with the Preferred Bidder, backed by a parent company guarantee, with the Arena operator matching the Council's obligations to the fund. In this scenario, the Council is effectively acting as a guarantor to the Arena operator in order to secure sufficient funding to build the Arena, with the commercial nature of operating an Arena giving sufficient confidence to enter into this income strip / lease and lease back arrangement at a net-nil cost to the Council. At the end of the 45 year lease arrangement, both the Arena and Travelodge assets will revert back to the Council. Approval of the final details of this arrangement will remain subject to a future Cabinet decision.
60. A key risk to the Council of entering into an income strip / lease and lease back arrangement is being exposed to the risk of arena operator default.

Significant mitigations have been agreed to minimise this risk as far as possible, but essentially if the arena operator (and their parent company who have provided a guarantee) fails during the lease period, the Council would still be required to make the annual rental payments to the financial institution, even if there is no matching payment from the arena operator. As this is a substantial financial risk, relevant due diligence and financial checks have been carried out on the proposed arena operator and the parent company offering the guarantee. Further, more detailed, financial due diligence will also be carried out in the coming months to monitor the financial position of operators ahead of any future contract award decision by Cabinet, and before entering into the Development Agreement.

61. Through competitive dialogue, bidders and financial institutions have also confirmed that to deliver the required capital stack to fund the Arena construction, the Council would need to sign up to income strip (the lease and lease back arrangements) at Financial Close (rather than Practical Completion). This approach brings with it additional risks for the Council, particularly at the construction stage, but also improves the achievable yield which helps the project become more financially viable. For example, in the circumstance that the developer fails during the construction period, the Council would still be required to make the rental payments due to the fund, irrespective of whether the Arena and Hotel development is completed. The Bidder would have similar obligations to the Council; however the Council would need to satisfy itself that the Preferred Bidder was able to meet these obligations (for example in the event of the Arena and hotel not being complete). There are mitigations the Council has insisted upon, including a parent company guarantee from the ultimate parent company of the Preferred Bidder to cover this practical completion risk and having rights allowing the Council to step in to complete the development (alongside an appropriate long stop date for practical completion), however, the Council needs to satisfy itself on whether these are sufficient in such an event.
62. As outlined above, the alternative to this approach is the use of an agreement for lease which obliges the Council to only pay rent under the occupational lease once the development has reached practical completion by a long stop date. However, the Council has been advised this would reduce the capital sum available to finance the project and therefore make the Arena unaffordable and undeliverable. The details of the agreement will become clearer once negotiations between all three parties can be concluded and a funding solution has been finalised. As referenced above, this will remain subject to a future Cabinet decision.
63. The income strip / lease and lease back element of the funding strategy is reliant on achieving the yield set out in the draft Heads of Terms, and this remains a key risk for the next stage of the project. Bidders have agreed HOT's with a proposed Funder (summary attached in Sections 3 and 5 of Confidential Appendix 2) and this forms the basis of the existing funding strategy. However, if funding markets and pricing substantially move between now and financial close, or if public sector credit ratings are negatively impacted to the extent there is a future downgrade to the Council's credit rating, this would have a significant impact on yields achievable and therefore the funding available to finance the project. (More

detailed explanation of impact of yield movements on the project can be found in Section 5 of Confidential Appendix 2).

64. It should be noted that any advantageous market movements between appointment of Preferred Bidder and financial close will have the effect of increasing the amount of capital generated from the income strip / lease and lease back deal, and this in turn will reduce the amount of gap funding the Council needs to provide to the development in the form of Council capital contribution. Any disadvantageous market movements will be the responsibility and risk to the preferred bidder. Whilst the risk of negative market movements sits with the bidder and is ultimately a risk for the developer, substantial market movements which reduce the capital stack available to deliver the Arena could have the effect of making the project unaffordable.

Preferred Bidder

65. A financial summary of the Preferred Bidder's proposal is included within Section 3 of Confidential Appendix 2. This sets out the maximum level of Council capital contribution required to deliver the Indoor Arena, the annual rental amount of the income strip / lease and lease back the Council will be guaranteeing (although this will be paid by the operator) as well as the amount of annual income the Council can expect to receive once the Arena is fully operational. Agreed 'Heads of Terms' with an appropriate funder are also included within Section 5 of Confidential Appendix 2 setting out the proposed terms of the income strip / lease and lease back deal, albeit this will remain subject to future market pricing movements.

Arena Affordability Envelope

66. In February 2019, as part of the budget setting process, Council approved an affordability envelope in the Council's Medium-Term Financial Plan to support delivery of a new Indoor Arena. This included financial provisions for land assembly, as well as other associated costs required to deliver the Indoor Arena and associated facilities. Details of the current projections against the agreed affordability envelope are set out within Section 7 of Confidential Appendix 2.

Council Obligations (Conditions Precedent)

67. To facilitate the Arena development there are a number of obligations placed on the Council (as set out in the Conditions Precedent) that will require financial contributions to achieve. These include the Council completing land acquisitions, release of covenants, stopping up orders, delivery of sufficient car parking in Atlantic Wharf etc. within appropriate timescales to fit with the Arena programme delivery. Some of these are relatively straightforward to achieve, whilst others will be more challenging. (Further details of these, along with an estimate of the financial costs of delivering these obligations, are set out in Confidential Appendix 1). Cabinet should review this confidential appendix, in order to be aware of the obligations the Council is required to deliver to enable the Arena development to be completed, and be confident this can be achieved to avoid potentially abortive costs at the

next stage. The programme delivery implications of any delays in achieving these obligations must also be noted.

68. Head of Terms have been agreed with ABP as per Confidential Appendix 5. This report includes a recommendation requesting delegated authority to complete these Heads of Terms with ABP, and this is supported by an independent advice note at Confidential Appendix 6 suggesting “*obtaining agreement in the said manner is commercially sensible from the Council’s perspective*”, with statutory appropriation of the land without the co-operation of ABP an option that be pursued only as “*a matter of last resort*”. The costs of entering into these Heads of Terms will be funded by utilising the Arena Affordability Envelope.

PCSA

69. As part of the next stage of the Arena Procurement the Council will be entering into a PCSA. This agreement details that the Bidder agrees to carry out further design development (to RIBA Stage 3 in order that all parties can have more confidence that the affordability envelope can be met, before the parties’ enter into the Development Agreement . This will mean the Council agreeing to underwrite the developer’s costs (up to a pre-agreed cap). Details of the developer cost underwrite at PCSA stage, along with the proposed cap, can be found in Section 8 of Confidential Appendix 2. However, it is important to note that these costs will become development costs to be covered by the Preferred Bidder if final approval is given to proceed. These costs only become payable by the Council in a scenario where bidders are able to meet agreed deadlines and remain within the current affordable envelope throughout, but the Council chooses not to proceed with the development.
70. Following the PCSA stage, further Cabinet approval will be required to proceed to award the contract (entering into the Development Agreement) to the Preferred Bidder. If signed, the Development Agreement will remain subject to the satisfaction of several conditions, and once these conditions are met, the Council will grant a lease to the developer or its funder and the income strip / lease and lease back arrangements will then be entered into at financial close. The conditions here include Planning, Restrictive Covenant, Site Assembly, Stopping Up, Hotel and Funding. If the Conditions are not met because of the Council’s failure to satisfy the Restrictive Covenant, Site Assembly or the Stopping-Up Conditions then the Council will be required to pay the developer’s costs up to a pre-agreed cap. Whilst Cabinet are not being asked to approve entering into the Development Agreement at this stage, it is important that Council have sufficient confidence that the conditions within the Development Agreement can be met in order to avoid potentially significant abortive costs at the next stage.

Travelodge Hotel

71. The land the existing Travelodge Hotel currently sits on forms part of the land required to deliver the Arena so will be included in the lease to be granted to the. Preferred Bidder at contract award stage, with the existing Hotel intended to be demolished and re-provided elsewhere on the Arena

site. This is required to facilitate the delivery of the Arena itself. The Council will remain as the freeholder of both the existing Hotel site, as well as retaining the freehold on the land on which the Arena and new Hotel will sit. A long lease (199 years with a break at year 45) will be granted to the funder, with further leases (45 years) will be granted to the developer/operator as part of the income strip / lease and lease back deal, with all the land and assets then due to revert back to the Council at the conclusion of the 45 year Arena lease.

72. In addition to the long-term impact described above, Cabinet must also be aware that the Travelodge entered into a CVA agreement with its landlords in June 2020 which has meant the rent previously agreed will be reduced in 2020 and 2021, and the asset has been significantly de-valued. As part of this CVA agreement the Council has the right to exercise a break clause for the existing Travelodge lease. This clause allows the landlord to break the lease agreement with Travelodge with no penalties, and effectively allows the landlord to exit the existing lease and consider alternative operators or other solutions. This presents an opportunity for Council in light of the importance of the Hotel in the Arena development, but also brings with it risks. Agreeing to break the lease will substantially de-risk delivery of the Arena project, but will come at a cost to the Council and have a significant impact on the Red Dragon Centre investment asset, with a potential long-term loss of lease income (if the Arena proceeds or not). (Please refer to Confidential Appendix 11 for further details in relation to this Travelodge Hotel decision, which is supported by independent advice from Cushmans and Avison Young at Confidential Appendices 8 & 9).

State Aid

73. State Aid is referenced in the report in the context of the Council's contribution to the construction of the Arena development. The Council has taken independent legal advice, set out in Confidential Appendix 1, which demonstrates how the Council could satisfy State Aid requirements regarding any public contribution towards the construction of the Arena. The grant agreement then provides for the Council's financial contribution to the costs of the Project by means of a grant up to a maximum sum (see Confidential Appendix 2, Section 3) to be drawn down during the construction phase based on a pro rata share with the funder, and in accordance with certificates of expenditure from an independent cost consultant. State aid is also present in the income strip/lease and Leaseback arrangement due to the additional value to the Developer of the Council's covenant which forms part of the financial contribution. State Aid rules dictate there will also need to be a reconciliation against actual costs incurred once the construction phase is completed so that the amount of the grant may be varied to reflect actual expenditure rather than estimates. The capital contribution figure set out in Section 3 of Confidential Appendix 2 therefore represents the maximum capital sum available to the developer, with any savings in delivery costs resulting in a reduced Council contribution.

Accounting and Tax Implications

74. The confidential appendices set out the preferred bidder's chosen funding model for delivery of the Indoor Arena, as well as independent advice on the proposed accounting and tax treatment the Council should apply, and the impact this could have. Details of proposed tax and accounting treatment, as well as key actions to progress at the next stage, can be found within Section 11 of Confidential Appendix 2. Further financial implications will be provided at the conclusion of the PCSA stage and ahead of a future Cabinet decision on contract award. At this point, the legal documents and structures being entered into will have been optimised and finalised between the Council and the Preferred Bidder, and the final position will be known. These future financial implications will include confirmation the chosen funding model is the most optimal solution, with a clear and robust understanding of the opportunities and risks associated with this funding model. It will also confirm the proposed accounting and tax treatment, ideally following early dialogue with the Council's auditors.
75. A transfer, or appropriation, of land including the County Hall Car Park and existing Travelodge Hotel will be required to facilitate this development and enter into the required Funding Agreements for the Arena with the preferred bidder. As these are currently Council assets, appropriating this land will have Balance Sheet implications for the Council. The Balance Sheet implications are initially considered in Section 11 of Confidential Appendix 2. For clarity, no Cabinet decision requiring the transfer or appropriation of land is sought within this report, and further more detailed tax and accounting implications will be provided within a future Cabinet report when a decision will need to be taken on this.
76. Initial VAT advice received by the Council on the status of Grant Funding suggests that any Council capital contribution may be subject to VAT. Therefore in order for the Council to recover this VAT the Council will be exercising an option to tax over the whole site, in order that any interests in land granted are taxable rather than exempt supplies. In principle, this would allow for VAT recovery on any costs directly associated with these interests. Similarly the Council has included a clause that stipulates bidders cannot dis-apply the option to tax in relation to the Land and will not do, or cause to be done, or omit to do anything which could lead to the option to tax being revoked or dis-applied by operation of law or otherwise. The Council intends to work with the preferred bidder to optimise their solution at the next stage, and further detailed tax advice will be sought to assist with this, including an intention to seek an early ruling from HMRC regarding the VAT liability of the Council's contribution to ensure correct tax treatment is implemented.

Legal Implications

Procurement

77. The Council received two Final Tender submissions prior to the Final Tender deadline.

78. Following the evaluation of Final Tenders in accordance with the evaluation criteria and methodology set out in the CFT the Council has identified a Preferred Bidder that provides the overall most economically advantageous tender.
79. Approval is now sought to appoint the developer/operator consortium identified as the Preferred Bidder who will be required to work with the Council to finalise the contractual arrangements and work up its designs to deliver the Arena and Travelodge hotel.
80. In appointing a Preferred Bidder the Council will be required to enter into a PCSA which will govern the relationship and expectations between the Council and the Preferred Bidder to progress the design from RIBA Stage 2 to RIBA Stage 3 in respect of the Arena and Travelodge hotel.
81. Entering into the PCSA will mean that the Council will be agreeing to underwrite the Preferred Bidders bid costs where conditions within the PCSA are met. A summary of the terms of the PCSA and the additional legal documents is contained at Confidential Appendix 1. A summary of the key risks in relation to those documents is contained at Confidential Appendix 14 and more detailed advice is contained in Confidential Appendix 15.
82. Whilst the appointment of a Preferred Bidder is a key milestone in the procurement process, it does not mean that the competition has concluded. Upon successful completion of the Preferred Bidder stage the Council will be required to seek further Cabinet approval to proceed to award the contract with the Preferred Bidder.

State aid

83. The Council has previously received advice on the state aid implications of the scheme, and the issues have been factored into the CFT documents. On the basis of the law as it stands at present the Council has been advised that the scheme will involve aid which is compliant with the State Aid rules under the Treaty on the Functioning of the European Union. At this stage the Council is not making a decision to award any benefit to the preferred bidder other than under the terms of the PCSA. The PCSA only confers a benefit in the event of the project not proceeding for defined reasons (see paragraph 31 above) and the Council has been advised that the terms of the PCSA represent a market position for this stage of a complex procurement, in that it would be unreasonable and uncommercial to expect the preferred bidder to carry the whole of the risk of the expenditure to be incurred during the period from appointment as preferred bidder to entry into the Development Agreement.
84. The UK government's current position (albeit subject to ongoing negotiations) is that the EU rules will cease to apply on 31 December 2020, and thereafter, pending a consultation on any new subsidy control mechanism, the UK government has merely committed to be compliant with the World Trade Organisation Agreement on Subsidy Control and Countervailing Measures. This only applies to restrict subsidies which affect the trade in goods and the Council has been advised that it would raise no

issues in relation to the Arena project. The position of the Government may change, and the recent trade agreement with Japan published on October 23 indicates a greater level of obligation, but it does not appear to give rise to any implication that the project would involve any breach by the Council of any relevant obligation. As stated in para 82 above, if the EU rules continue to apply at the point of award of the contracts, the Council has been advised that the proposed financial support is compliant with the EU state aid rules.

Powers

85. Section 120 of the Local Government Act 1972 enables the Council to acquire land for either (a) the benefit, improvement or development of its area or (b) for any of its functions under any enactment.
86. Section 145 of the Local Government Act 1972 enables the Council to do, or arrange for the doing of, or contribute towards the expenses of the doing of, anything necessary or expedient for the provision of entertainment of any nature or the provision of a theatre, concert hall, dance hall or other premises suitable for the giving of entertainments and any purposes incidental to that provision.
87. Section 12 of the Local Government Act 2003 enables the Council to invest (a) for any purpose relevant to its functions under any enactment or (b) for the purposes of the prudent management of its financial affairs.
88. The Cabinet needs to take account of the Council's fiduciary duties to the local residents and taxpayers. As such, proper consideration needs to be given to the risks, rewards and potential future liabilities of the proposals which are the subject of this report. The issue concerns whether the potential risks and liabilities described in the report and in Confidential Appendix 15 are proportionate to securing the stated economic development objectives and thereby in the best interests of the local taxpayers and residents. Any viable alternatives for delivering the economic development objectives should be considered. Further legal advice is provided in Confidential Appendix 15.
89. In Cabinet must also make its decision having due regard to the Council's public sector equality duties pursuant to the Equality Act 2010 (including specific Welsh public sector duties). This requires the Council, in the exercise of its functions, to have due regard to the need to (1) eliminate unlawful discrimination, (2) advance equality of opportunity and (3) foster good relations on the basis of protected characteristics. The protected characteristics are: age, gender reassignment, sex, race - including ethnic or national origin, colour or nationality, disability, pregnancy and maternity, marriage and civil partnership, sexual orientation, religion or belief – including lack of belief. If the recommendations in this report are accepted and when any alternative options are considered, the Council will have to consider further the equalities implication and an Equality Impact Assessment may need to be completed.
90. Equalities impact assessments will be undertaken as necessary as the proposals described within this report are developed,

91. The Well-Being of Future Generations (Wales) Act 2015 (“the Act”) places a ‘well-being duty’ on public bodies aimed at achieving 7 national well-being goals for Wales – a Wales that is prosperous, resilient, healthier, more equal, has cohesive communities, a vibrant culture and thriving Welsh language, and is globally responsible.

In discharging its duties under the Act, the Council has set and published well-being objectives designed to maximise its contribution to achieving the national well-being goals. The well-being objectives are set out in Cardiff’s Corporate Plan 2020-23: <http://cmsprd.cardiff.gov.uk/ENG/Your-Council/Strategies-plans-and-policies/Corporate-Plan/Documents/Corporate%20Plan%202018-21.pdf>

92. The well-being duty also requires the Council to act in accordance with the ‘sustainable development principle’. This principle requires the Council to act in a way which seeks to ensure that the needs of the present are met without comprising the ability of future generations to meet their own needs. Put simply, this means that Council decision makers must take account of the impact of their decisions on people living their lives in Wales in the future. In doing so, the Council must

- Look to the long term;
- Focus on prevention by understanding the root causes of problems;
- Deliver an integrates approach to achieving the 7 national well-being goals; and
- Work in collaboration with others to find shared sustainable solutions;
- Involve people from all sections of the community in the decisions which affect them.

93. The Cabinet must be satisfied that the proposed decision accords with the principles above; and due regard must be given to the Statutory Guidance issued by the Welsh Ministers, which is accessible using the link below: <http://gov.wales/topics/people-and-communities/people/future-generations-act/statutory-guidance/?lang=en>

94. The Council has to be mindful of the Welsh Language (Wales) Measure 2011 and the Welsh Language Standards when making any policy decisions and consider the impact upon the Welsh language.

HR Implications

95. There are no HR implications arising from this report

Property Implications

96. The Strategic Estates Department have assisted and advised on certain property matters where necessary in respect the proposals to deliver and operate a new Indoor Arena at Atlantic Wharf, Cardiff Bay. There are no specific property implications in respect of this report. However, where there are resultant land transactions, or further negotiations or valuations required to deliver any proposals, they should be done so in accordance with the

Council's Asset Management process and in consultation with Strategic Estates and relevant service areas.

RECOMMENDATIONS

Cabinet is recommended to:

1. Appoint the Preferred Bidder developer/operator consortium as identified in Confidential Appendix 1 for the development and operation of a new Indoor Arena and Travelodge Hotel at Atlantic Wharf, Cardiff Bay.
2. Agree to enter into a Pre-Contract Service Agreement ("PCSA") with the Preferred Bidder including approval of the associated cost underwrite as set out in Confidential Appendix 2 (Section 8), subject to Confidential Appendix 15.
3. Delegate authority to the Director of Economic Development in consultation with the Cabinet Member for Investment & Development to negotiate Heads of Terms with the Preferred Bidder in relation to the Development Agreement and to return to Cabinet for approval alongside the Full Business Case in summer 2021.
4. Delegate authority to the Director of Economic Development in consultation with the Cabinet Member for Investment & Development to complete the land acquisitions as set out in the land strategy attached at Confidential Appendix 3, including the negotiation and completion of the Agreement with ABP to release the restrictive covenant and permit the Arena to be built adjacent to the dock feeder in line with the Heads of Terms and independent valuations contained within the Appendices to this report; and the acquisition of the freehold interest in the former Pizza Hut site on Hemingway Road.
5. Delegate authority to the Director of Economic Development in consultation with the Cabinet Member for Investment & Development to negotiate terms with Travelodge and to return to Cabinet for approval of an Agreement for Lease, or as necessary, serve notice on Travelodge to avoid Compulsory Purchase Order implications at the break date.
6. Note the obligations that will be placed on the Council when Cabinet considers the Full Business Case in the summer 2021 as set out in the Conditions Precedent document contained within Section F of Confidential Appendix 1.
7. Approve the additional project budget as set out in Confidential Appendix 2 (Sections 6) to progress delivery of the Indoor Arena project to the next stage.

SENIOR RESPONSIBLE OFFICER	Neil Hanratty Director of Economic Development
	20 November 2020

The following appendices are attached:

Appendices 1 – 15 of this report are not for publication as they contain exempt information of the description contained in paragraphs 14 and 16 of part 4 and paragraph 21 of part 5 of Schedule 12A of the Local Government Act 1972

Confidential Appendix 1 - Procurement Report MOTTS
Confidential Appendix 2 - Finance Report
Confidential Appendix 3 - Land Strategy Report
Confidential Appendix 4 - Car Park Proposal
Confidential Appendix 5 - HOTS ABP
Confidential Appendix 6 - Independent Valuation ABP
Confidential Appendix 7 - HOTS Travelodge Hotel
Confidential Appendix 8 - Independent Valuation Travelodge Hotel
Confidential Appendix 9 - Independent Appraisal Atlantic Wharf Masterplan
Confidential Appendix 10 - Financial Review of the RDC Investment
Confidential Appendix 11 - Legal Note on Travelodge CVA
Confidential Appendix 12 - RDC Tenants Report
Confidential Appendix 13 - Independent Financial Report
Confidential Appendix 14 - Legal Summary
Confidential Appendix 15 - Legal Advice