

Octagon Project Update

Executive Member(s): Lead Member for Communities, Housing and Culture, Cllr Federica Smith-Roberts

Local Member(s) and Division: All

Lead Officer: Executive Director – Communities, Chris Hall

Author: Chris Hall

Contact Details: chris.hall@somerset.gov.uk

1. Summary

- 1.1 This report is a position update following the approval by the previous South Somerset Council of the capital scheme and further work in preparation for contract award.
- 1.2 The report identifies a range of issues that have emerged since the original business case was approved. Given these issues further work needs to be brought forward to achieve and secure assurance of the full case and options.
- 1.3 The report sets out the financial pressures in both revenue and capital resources during the pre-construction, and construction phases.
- 1.4 The report sets out further financial pressures due to the increased borrowing costs and it is no longer possible to give assurance to Members that the future taxpayer funded revenue costs can be met. Based on current interest rates, these costs would increase significantly and present a new MTFP pressure in the region of £900k pa.
- 1.5 The report is not critical of the previous Business Case or the decision of South Somerset District Council; the conditions have changed beyond those that could reasonably have been foreseen at the time of approval.
- 1.6 The Octagon Board have been briefed on the issues.

2. Recommendations

2.1 The Executive:

- a) Confirms its commitment to the Octagon project as a flagship venue to deliver arts and culture services in Yeovil for Somerset

- b) Acknowledges that the current business case can no longer be met, and a revised business case would be necessary.
- c) Acknowledges the revenue financial pressure created by the works to date and instructs Officers to explore mitigations to these costs.
- d) Instructs officers continue to work with Department for Culture Media and Sports (DCMS) and Arts Council England (ACE) to find a viable Octagon business case to deliver cultural services in Yeovil for Somerset.
- e) Instructs work to be overseen by the Octagon Theatre Redevelopment Project Board in collaboration with all partners.

3. Reasons for recommendations

- 3.1 The approved business case can no longer be met, and assurances cannot be provided to Members that it could be met in the future.
- 3.2 Interest rates payable on the borrowing needed for the project have increased way beyond the approved business case. Alternative funding options have not been forthcoming and interest rates forecasts will remain in excess of the business case for the foreseeable future.
- 3.3 Whilst the current scheme is not affordable because of increased borrowing costs, there may be an opportunity to work with DCMS and Arts Council and other partners to find a viable Octagon business case to deliver cultural services in Yeovil for Somerset.

4 Actions taken

- 4.1 The following are actions that have been explored in the hope of provided some mitigation and enable delivery of the approved business case. Only 4.2, 4.3 and 4.8 are being taken forward.
- 4.2 Considerable effort has been put to challenging the costs and seeking measures to mitigate the cost growth. There may be options to reduce the capital build costs through value engineering. This needs to be undertaken sensitively, a reduction in the specification can lead to poorer build quality, higher operating costs, and potential challenge from DCMS with a reduction in their funding. Whilst it may be possible to design out the current predicted capital pressure of £1.7m the borrowing cost pressures remain. An entirely different scheme could be scoped to bring the theatre back into use. A cost estimate was provided for this which was in the region of £9m. Detailed modelling on this has not been progressed as this is a departure from the Member approved scheme and would require project resources and time to bring forward.

- 4.3 Request additional funding from DCMS and / or Arts Council England (ACE) – We have met with representatives from DCMS and ACE. We all have the desire to continue the delivery of the scheme but acknowledge the financial pressures. They have confirmed that there is no headroom in their capital programme and additional funding from them is not an option. They have also confirmed that the £10m of grant funding is specific for the approved business case. If we fail to meet all of the criteria, then the award is not guaranteed. This may prevent us from making changes to the scheme and retaining the full £10m grant.
- 4.4 Pausing / deferring the scheme – This would be in the hope of borrowing cost reductions. External advice has not given any indication of a return to rates that would fall within the approved business case. An indefinite pause would lead to the loss of the DCMS grant and places the council in a similar position to a decision to cease works.
- 4.5 Seek an alternative operator on a nil cost contract. – On completion of the scheme the new facility may have commercial interest from other operators, and it could be put to market with a stated expectation of no taxpayer contribution. However, to prevent any cost to the Council a future operator would need to meet the financing costs of Somerset Council, estimated at £1.435m (£380k MRP + £1055k interest) per annum which reflects the borrowing and Minimum Revenue Position (MRP). It seems unlikely that this could be achieved, and Somerset Council would continue to hold the financial risk. Timing is also a risk as a decision to proceed with the construction is needed before Christmas 2023, but it would take at least a year to run the procurement exercise for an operator. The time necessary and the retained financial risk have caused this option to be dismissed.
- 4.6 Proceed at risk – this would require Members to approve a revised business case with an increased operating cost pressures being placed into an already challenging MTFP horizon. There are no Somerset Council budgets that could contribute to the increased revenue costs without reducing or ceasing activity of a similar value, and for this reason proceeding at risk could not be recommended.
- 4.7 Divert the revenue contribution allocated to the Westlands Entertainment Venue – This would have a significant impact on the Westlands operation. Whilst we gave this some initial consideration it would require a separate Member approval. Whilst a diversion of this funding would provide some support, the Octagon budget pressure remains significant and therefore closure is not being proposed as a solution. We would also have a lost opportunity for the future use of the Westlands site.
- 4.8 Future options appraisal – proposed within the recommendations.

5. Links to Council Plan and Medium-Term Financial Plan

- 5.1 The Council is committed to the delivery of cultural services, these must be balanced with the approved business case, the immediate project deliverability, and long-term cost of operation at the taxpayer expense.
- 5.2 The development of a flagship theatre not only links to the delivery of cultural services but the economic regeneration of Yeovil and the whole of Somerset due to the added benefits the theatre added to the local economy.
- 5.2 The council's MTFP identifies a considerable budget gap. Changes to service delivery across the Council will likely be needed to meet this gap. Should Members reject the recommendations of this report there is no clear funding strategy for the project or the ongoing operation of the facility.
- 5.3 It will take time to fully understand the impact of revenue and capital money already spent. Some of this may be mitigated by a project specific capital reserve and other fundraising. Whilst the impact is not known in full it does not override the recommendations or justify continuing with a capital scheme where the evidence shows this to be unaffordable.

6. Financial and Risk Implications

- 6.1 Only one bid was received when the design and build contract was put to the market. Whilst we acknowledge there are a range of pressures in external contracting we should consider if the risks associated with this project and a constrained budget contributed to the lack of interest. Feedback from one of the anticipated bidders was that they did not believe the scheme was deliverable for the budget and so declined to participate.
- 6.2 Current capital cost estimates demonstrate that the budget will overspend by £1.7m. There are options being explored to reduce this cost through value engineering. Somerset Council will carry the risk if value engineering options cannot be made. There may be further risk if options selected increase operating costs through shorter component lifecycles, or do not meet with the approval of DCMS as a key funder of the project.
- 6.3 The modelling on revenue costs has been undertaken with a number of assumptions, as with any business case this creates an indication as to the likely financial performance of the operation. The updated business case reflects the known changes in the borrowing costs but does not revise any of the other previous assumptions. The headline changes are as follows:

Initial Business case	Modelled position
Total scheme costs £29,010,000	Capital costs estimates £30,710,000
Other funding available £2.25m	Reduced to £1.312m
Borrowing need £16,318,000	Revised borrowing £18,978,000 *
PWLB rate of 1.5%	PWLB (August '23) 5.56%
Annual interest repayments c£245k	Increased to c£1,055k *
MRP at 2% = £326k pa (reducing)	MRP at 2% of new borrowing total = £380k pa (reducing)
Net revenue cost removed by year 6 (2030/31)	Net revenue cost removed by Year 23 (2048/49) *
Assumed use of existing internal resources	Internal resources are not sufficient to deliver a project of this value or complexity (increase cost £100k pa)

*The borrowing costs are based on capital estimates, any increase identified in the seconds stage tender would increase these costs further.

- 6.4 Revised financial modelling with the above assumptions demonstrates that the on-going revenue cost to the Council would rise from £130k in the approved business case to as high as c£930k per annum plus a further £100k pa of additional resources during construction. The main impact on the business case will be the cost of borrowing which has increased from an estimated 1.5% at the point of approval of the business case to the current rate position of 5.56% (August 23) if fixed for 50 years. Council could consider taking short-term borrowing and seek to fix costs in future years in the hope of more favourable terms. However, the short-term borrowing would likely cost more in those initial years.
- 6.5 External Treasury Management opinion suggest that interest rates may reduce to 4.4% by the end of Q4 24/25. This is still nearly three times the rate approved and whilst it is a better position than current rates it would continue to be unaffordable within the business case.
- 6.6 At the point of the original approval the borrowing costs could not have been foreseen to rise in the way they have, similarly it is not possible to give any confidence on the future borrowing costs and so the modelling uses a fixed rate. For every 0.25% the PWLB rates increase the interest repayments increase by c£50k pa in the early years, this reduces with future MPR payments over the 50-year borrowing term.

- 6.7 In developing the design, undertaking the survey works and going through the procurement process there have been costs that are incorporated into the capital budget. Should the project not progress into a capital scheme these costs will change from capital to revenue as part of the necessary accounting practice. Expenditure to date on a range of preparatory works is £1.77m, and the surveys have advised that no RAAC has been identified.
- 6.8 The recommendations of this report are for officers to seek financial mitigations that limit impacts on the revenue budget.
- 6.9 Project specific risks are managed through the Octagon Project Board
- 6.10 Following discussions with DCMS and ACE there are no risks to the National Portfolio Status or funding provided.

7. Legal Implications

- 7.1 The Council is under no obligation to award the contract on receipt of the final tender price.
- 7.2 There are a number of external funding streams that have been allocated to the project. Officers will need to work with organisations that have offered those funds to confirm if they can be passed to an alternative scheme, this will only be known for certain once options have been identified and negotiations undertaken.
- 7.3 DCMS and ACE have clarified their position, and no funding can be drawn down from the grant without Council accepting the increase borrowing costs. No DCMS grant has been received to date, Somerset Council are liable for expenditure to date.

8. HR Implications

- 8.1 The planned closure of the Octagon as part of the pre-construction survey work led to a diversion of staffing resources to Westlands, and less reliance on our casual workforce. There were no redundancies identified as part of this work.
- 8.2 If the recommendations of the report are accepted this would continue to be the position whilst an options appraisal is undertaken.

9. Other Implications:

Equalities Implications

9.1. The recommendation of this report is to seek alternative ways to deliver arts and cultural services, there are no recommendations as to how this is done at this stage and so equalities impacts cannot yet be fully assessed. The Octagon theatre cannot be reopened and will remain closed whilst these options are being explored. Wherever possible services have been transferred to the Westland site. The original business case addressed long standing accessibility issues on the site.

Community Safety Implications

9.2. Intrusive survey works have been undertaken within the building and reopening is not an option without further money being spent. If the recommendations of the report are followed the building will remain closed to the public pending further options being worked up with DCMS and ACE. The site is currently secured but could become a future target for vandalism or urban explorers.

Climate Change and Sustainability Implications

9.3. Somerset Council have declared both a Climate and Ecological Emergency. Through that, the Council has committed to working towards making the whole county, including our own estate and operations, 'Carbon Neutral' by 2030 and to take positive action to reverse the damage on our natural habitats by human-caused activity. We have also pledged to ensure that Somerset is resilient to, and prepared for, the effects of Climate Change.

9.4. The capital improvement scheme would have delivered a fully decarbonised facility. If the recommendations of the report are accepted officers will need to consider this as part of the future options appraisal.

Health and Safety Implications

9.5. With more time now needed to consider options for future delivery the building being unused for an extended period.

Health and Wellbeing Implications

9.6 There are no immediate implications from this report. The original business case did however demonstrate that Culture supports the preventative agenda for increasing better health and wellbeing outcomes.

Social Value

9.7 Social value was considered as part of the procurement process.

10. Scrutiny comments / recommendations:

10.1 Given the urgency in bring this report to Executive it was not possible to have the item considered by Scrutiny Committee – Communities in advance. The report and presentation were discussed with the Chair and Vice Chair on 18 September 2023.

11. Next Steps

11.1 The following are a list of in-train and planned activities that result in new report for the Executive to consider. The date of that report will depend on the complexity of the options and the timeline of other funders:

- Octagon Board briefing 13th September
- Yeovil Town Council officer meeting, and ongoing support
- Media interview and roll out of communications strategy
- Executive 4th October
- Media and stakeholder visits to Octagon
- Build and financially assess options with DCMS
- Executive report with options appraisal

12. Background Papers

Appendices

- **South Somerset District Council approved Outline Business Case (OBC)**

Report Sign-Off

	Officer Name	Date Completed
Legal & Governance Implications	David Clark	14/09/23
Communications	Chris Palmer	14/09/23
Finance & Procurement	Nicola Hix	14/09/23
Workforce	Alyn Jones	14/09/23
Asset Management	Oliver Woodhams	14/09/23
Executive Director / Senior Manager	Chris Hall	14/09/23
Strategy & Performance	Alyn Jones	14/09/23
Executive Lead Member	Cllr Smith-Roberts	14/09/23
Consulted:		
Local Division Members	Various	18 th & 19 th Sep
Opposition Spokesperson	Cllr David Fothergill / Cllr Andy Dingwall	14/09/23
Scrutiny Chair	Cllr Wren	18/09/23