AGENDA ITEM 10

FALKIRK COUNCIL

Subject: **FALKIRK COMMUNITY STADIUM LIMITED: DEMERGER PLAN**
Meeting: **FALKIRK COUNCIL**
Date: **4TH MARCH 2009**
Author: **CHIEF EXECUTIVE**

1. INTRODUCTION

1.1 This report provides Members with a further update in respect of the restructuring proposals previously presented to Council in a report on the outcomes of the strategic review carried out by Falkirk Community Stadium Ltd (FCSL). The review covered all aspects of its operations and concluded by setting out a proposal to restructure the existing arrangements to provide a robust and sustainable platform for future operation and development. At its meeting on 22 September 2008 Council previously approved, in principle, the restructuring proposals. This report recommends that Members now approve the demerger plan.

1.2 This report addresses the areas identified in the earlier report that required further detailed consideration and provides more information on the implications for the Council. It advises that the Council will take full ownership and control of the West Stand along with much of the work of the existing FCSL including its staff. Falkirk Football and Athletic Club (FFAC) will be responsible for the existing football assets and for the future development of the East Stand.

2. BACKGROUND

2.1 Members will recall that in August 2008 FCSL submitted a detailed proposal to its shareholders for consideration. It advised that the FCSL Board had carried out a strategic review and that three options were evaluated against three strategic criteria:-

- Delivering a completed Stadium and site development
- Repaying the loans from Falkirk Council
- Ensuring financial sustainability of the ongoing operation

2.2 The previous report to Council advised that the Board of FCSL had suggested that the most appropriate means of achieving the strategic objectives was through a reorganisation of the company in a commercially attractive and tax efficient manner. It proposed a detailed split of the assets and recent work has focussed on working through the detailed implications for FCSL, FFAC and the Council of the demerger plan. This work has been taken forward through a working group drawn from representatives of each organisation as well as each party taking independent advice when necessary.

2.3 Members previously agreed that whilst the Council was supportive in principle of the proposals more detailed work was required in the following areas:-

- Assessing the fair distribution of assets in the context of the District Valuer's involvement.
- Working on the delivery of the master plan for the successful development of the Stadium site.
- Reaching agreement on the management and responsibilities of the shared assets.
- Establishing the revenue implications associated with the asset transfer.
- Developing appropriate legal agreements to reflect the new arrangements.

2.4 The demerger plan will effectively split FCSL into three new companies with the assets and activities being allocated appropriately to the Council and FFAC. One of the newly created companies will be wholly owned by the Council, one will be wholly owned by FFAC and one will be set up to take the football assets and shares in FCSL initially and then it will be liquidated to transfer assets and shares to the other companies. This will result in the Council taking responsibility for all the existing commercial activities (including all non-football tenancies in the West Stand) and for the development of the entire site excluding stands. FFAC would take responsibility for all the football related areas including the West and North Stands (excluding non-football activities in the West Stand), pitch, floodlights and for the development of the South and East Stands. This split allows both shareholders to concentrate on their own core activities. The table below summarises this.

Falkirk Council New Co3 ***Assets***	***FFAC New Co2*** ***Assets***
West Stand Conference Centre Five-a-Side Football Third Party Leases Development Plots	Leases: West Stand Footballing Areas Ground Lease – Pitch, North Stand, South Stand, East Stand Plot
Responsibilities	***Responsibilities***
Management of Conference Centre Five-a-Side Football Management Third Party Leases Management Communal Areas Service charge Development and Collection West Stand Maintenance and Development Development Agreement for corner pods and associated developments	Development of football related assets in West Stand North Stand East Stand development South Stand development Pitch Maintenance Share external maintenance of West Stand
People	***People***
16 staff in full and part-time posts	None - FFAC to decide on Management

3. DETAILED CONSIDERATIONS

<u>West Stand Ownership Model</u>

3.1 Members may recall that FCSL originally proposed that the Council and FFAC share ownership of the West Stand. However, when the joint working group considered this in more detail, it became apparent to both parties that it would be more appropriate to identify a single owner and for the other party to have a lease with such obligations as to mirror ownership. It was considered that as the Council is landowner and landlord it was best placed to take full ownership of the West Stand and for FFAC to have a long term lease. The proposed lease gives each party a 50/50 share of the exterior maintenance liability. FFAC will also have a pro rata share of the internal maintenance and operational liability through their share of the service charge. After full consideration it has been concluded that it makes sense for the Council to be the sole owner and for FFAC to have a lease within the West Stand because of the other lease interests that the Council would already have as a consequence of the demerger plan. This is in keeping with the previously identified asset split.

3.2 It is proposed that the allocation of the football assets that are transferring to FFAC be done by way of two leases, each for a period of 169 years being the period to the end of the original ground lease. The first lease will be for the areas within the West Stand described above and shown in Appendix 1 (a) to (d). As stated above the terms of the lease require the club to share in the external maintenance costs and to contribute through the service charge to the ongoing costs of operating the west stand. The second lease will be a ground lease for the areas of ground that accommodate the pitch, the North Stand and the South Stand along with the plot for the future development of the East Stand. The Club will be fully responsible for the maintenance and management of the pitch and the stands and for the future provision of the East Stand. The lease also identifies that no commercial development can take place on the East Stand plot without the construction of a permanent stand. The areas covered by this lease are shown in Appendix 2.

<u>Assessment of the Fair Distribution of Assets</u>

3.3 One of the issues identified in the previous report was the distribution of assets. In practical terms this concerned the split of the West Stand between the footballing areas and the areas not currently identified for commercial lease (the current FCSL offices, the conference centre, the stadium control room and support facilities). In view of the specialist and complex nature of the valuation required the Council has taken additional external specialist advice from a valuer with specific knowledge of football related assets. This indicates that the relative worth of assets transferring to the Club and Council is broadly similar thus supporting the original FCSL proposal that the asset value of the West Stand be split on a 50:50 basis. It is accordingly considered that this represents a fair and equitable distribution of this asset.

3.4 The other assets transferring to the Council including the development plots, the third party leases and the five-a-side football centre valuations are unchanged from the previous report. Whilst the market conditions have changed dramatically in the last six months and current day valuations would be likely to be below the previously reported level the deal still represents the best value option for the Council. The Council is still receiving the appropriate share of the overall assets. With those assets in its sole ownership it is better placed to decide how and when to maximise the opportunities arising from its investment in the Stadium from the economic development, commercial management and community engagement perspectives.

<u>The delivery of the Masterplan for the Wider Site Development</u>

3.5 The FCSL proposal suggested that the development plots within the current FCSL ground lease including the corner pods be allocated to the Council as part of the asset split. Since the last meeting officers have been in dialogue with Henry Boot Developments Ltd to take forward detailed Heads of Terms governing the outline masterplan previously considered. However, with the current economic market conditions impacting on potential tenant demand and availability of finance this work is not yet concluded. There are, moreover, procurement issues that require to be worked through before making further progress. These matters will be progressed further as development options become more certain.

3.6 In the previous report officers noted that further work was also required on the indicative infrastructure costs associated with the proposed outline masterplan. Early indications suggest that the costs may be nearer £1.7m rather than £1m suggested by FCSL. However, this is an estimate only and will be refined further in the detailed discussions with the developer. The extent to which such costs might impact on the level of net capital receipts will be addressed through consideration as to the Council's support for the phased drawdown of land for development. This will be on the basis of finalised Heads of Terms which will require the Council's agreement and will be a critical factor for the best price/best value assessment. As previously stated it will be very important for the Council to consider carefully each disposal as it arises in order that best value criteria are properly satisfied.

3.7 The main issue for Members to consider at this stage is that the future development potential of the site will be in the sole control of the Council.

Reaching Agreement on the Management and Responsibilities of the Shared Assets

3.8 As outlined in paragraph 3.1 it is proposed that the West Stand will be managed by the Council through a lease with FFAC. This covers both the internal and external West Stand areas. The day to day management of the communal areas will be achieved through an operating model similar to the current FCSL management arrangements. It is proposed that, along with the transfer of the physical assets, the work in managing those assets and the staff who undertake the work should be encompassed in the new Council owned company.

3.9 FFAC will need to make appropriate arrangements for the management of the assets transferring to them and it may be that they will initially seek to share some services with the Council owned company e.g. building security and call out arrangements with the costs recovered from the Club.

Revenue Consequences of the Asset Transfer

3.10 One of the key aspects of the current work has been to make an assessment of the financial implications for the Council arising from the demerger plan.

3.11 The loans advanced by the Council of £5.095m are estimated to be around £6.160m as at March 2009 as a consequence of the capitalisation of interest throughout the deferred period. These loans will cease to exist, with the Council receiving alternative assets in lieu of the sum outstanding. The Council will bear the loan charges accruing on this balance until value can be released from the development plots. This cost has been incorporated into the 2009/10 budget. Other sums owed by FCSL in respect of professional fees and payroll costs will remain outstanding, until recovered through the future development value of the assets transferring to the Council.

3.12 The Council will own the West Stand through its wholly owned company (New Co 3), as well as the five-a-side pitches. Using the FCSL Management Accounts for the 7 months to December 2008, the Director of Finance has projected the 2009/10 income and expenditure of FCSL to be as follows:-

	£'000	***£'000***
Income		
Rents		198
Service Charge		224
Five-a-Side		131
Conferencing		38
Other Income		6
		597
Expenditure		
Employer Costs	308	
Other Expenditure	301	609
NET EXPENDITURE		12

3.13 The budgeted net operating position is likely to be very small and will be absorbed within the budget for Community Services. During the review period referred to in paragraph 3.17 the Council would be responsible for meeting any day to day cash flow requirements of the Council owned company.

3.14 It is worth noting that FFAC will be responsible for the revenue consequences of the assets transferring to them.

Developing Appropriate Legal Agreements to Reflect the New Arrangements

3.15 As previously stated the main legal agreements in respect of future operation of the stadium are the leases setting out the relationships between FFAC and the Council. In addition, a series of legal documents enabling the demerger to be formally carried out are being prepared by the legal advisers. These will enable the formation of the companies to take the new assets and to ensure the legal transfer of the responsibilities and liabilities accordingly. This has been a detailed and complex exercise and has included securing appropriate clearance from Her Majesty's Revenue and Customs (HMRC) for the members' voluntary liquidation of FCSL.

3.16 As stated previously the main consideration for Members has been the appropriate formation of the new Council owned company with specific responsibility to develop and manage the assets being transferred. The company has been properly set up and is able to comply with company law in the execution of the duties set out. The Council will be required to appoint directors to the new company; it is proposed that the current Council FCSL directors fulfil this role meantime. The company will have 16 people (13.4 fte) in a combination of full and part time positions each of whom are currently employed by FCSL.

3.17 However, it is proposed that a review of the Council owned company be carried out within a year of its establishment to determine whether the company should be retained or if its work would be better integrated within the general work of the Council and efficiencies achieved as a result. As Members are aware the Council has significant expertise in managing and delivering development opportunities, managing business tenants in a range of locations and in providing a diverse range of leisure services across the Council area. It may be that greater integration would offer benefits and therefore it is suggested that this be explored further once the Council has been operating the company and has a better understanding of the associated issues.

4. LEGAL IMPLICATIONS

4.1 Members will recollect the legal advice from Morton Fraser which was set out in the September report. This dealt with the broad outline of the demerger proposals and concluded that, while they were not without risk, they nevertheless made the best contribution to achievement of the strategic objectives which were referred to in the report. That position has not changed and Morton Fraser has continued to be involved in advising the Council and developing the legal agreements referred to above.

4.2 As FCSL will remain as a stand alone company, albeit wholly owned by the Council, those employees referred to in paragraph 3.16 will remain within the employment of the company. If the work undertaken by that company is subsequently transferred at any stage then the potential for TUPE transfers may arise. This will be fed into the review referred to in paragraph 3.17.

4.3 As far as the development sites are concerned further consideration still requires to be given to the procurement options as they develop, to ensure the Council complies with statutory responsibilities.

5. CONCLUSION

5.1 The group set up by FFAC, FCSL and the Council to work through the detailed consequences of the demerger plan have gone through the current operational model and legal arrangements to clearly establish the future roles, remit and responsibilities of the new companies being set up under the ownerships of FFAC and the Council. Appropriate clearances have been obtained from HMRC to enable the members' voluntary liquidation to proceed and the associated legal documentation is being prepared.

5.2 It is proposed that the FFAC interests be encompassed in two leases, one in respect of the West Stand football assets and one in respect of the ground lease covering the pitch, North Stand, South Stand and future development area for the East Stand. It is proposed that the Council will have a wholly owned company responsible for the West Stand, the conference centre, the five-a-side football centre, the third party leases. It will also take forward negotiations on the completion of the future development sites including the corner pods.

5.3 The new Council owned company will undertake much of the work of the current FCSL and will employ the staff currently based at the stadium. It is proposed that a review of the company be carried out within a year of its formation to ascertain if efficiencies can be achieved through greater integration with similar Council services.

5.4 Given that Members have previously agreed in principle to the demerger and reorganisation arrangements it is suggested that as the areas of further detailed work have not identified any new or additional risks Members should now give formal approval for the demerger plan to be implemented.

6. RECOMMENDATIONS

6.1 It is recommended that Members:-

i. **Approve the restructuring of FCSL to form 3 new companies and the subsequent transfer of assets to the new companies which will be wholly owned by FFAC or the Council;**

ii. **Agree that the company wholly owned by the Council retain the current FCSL Council directors as its company directors (i.e. Directors of Development Services, of Community Services and Head of Accountancy);**

iii. **Agree that a review of the new company be undertaken within a year of its formation and a further report be prepared in this regard for Members' consideration;**

iv. **Note that a further report will be presented on the issues associated with taking forward the proposed Heads of Terms with Henry Boot Developments Ltd; and**

v. **Authorise the Chief Executive to take such action and to agree the terms of such documentation as is required to give effect to the foregoing.**

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Chief Executive

Date: 25th February 2009.

Contact: Mary Pitcaithly, Chief Executive. Ext. 6002.

LIST OF BACKGROUND PAPERS

1. Ryden's Report re Falkirk Stadium for Falkirk Council dated 11th January 2009.

Items not for publication on the grounds that they involve the disclosure of exempt information as defined in paragraphs 6, 8, 9 and 12 of Part 1 of Schedule 7A of the Local Government (Scotland) Act 1973.

Any person wishing to inspect the above background papers should telephone Falkirk 01324 506002 and ask for Mary Pitcaithly.