

15 Grant Funding of Galway's Art House Cinema

- 15.1** The Department of Culture, Heritage and the Gaeltacht (the Department) launched the second Arts and Cultural Capital Enhancement Support Scheme (ACCESS II) in 2006. The scheme was established to provide organisations with funding to build new or to redevelop existing cultural infrastructure.
- 15.2** A private company, Solas-Galway Picture Palace Teoranta (Solas), applied for funding under the ACCESS II scheme in 2006 with the objective to establish a specialist art house cinema in Galway city.¹ The planned cinema complex outlined in the funding proposal was to include three screens with a total of 276 seats, a bar/restaurant and a book shop. It was planned for the project to commence in spring 2007 and to be completed in two years. Despite provision of financial assistance from public funds totalling €8.4 million, the cinema is not yet available to the public.
- 15.3** This report examines the
- administration and management of the project
 - funding and payments made by the Department and other public bodies related to the new cinema.
- 15.4** A timeline of the main project events is set out in Annex 15A.

Business case for the project

- 15.5** Solas made the application for funding in November 2006. The grant application process required that the application be made in a prescribed manner, with projected cash flows and other supporting documentation which together formed the business case for the development of the art house cinema, and for the proposed State grant funding. The business case included a statement of the purpose of the project, project location, legal status of the promotor, the project management team and other parties involved in the project. The total grant requested from the Department was €4 million.
- 15.6** The business case stated that the total projected costs to design, build and fit-out the building would be €4 million. This projection was based on a pre-tender estimate using planned architect designs, costed by quantity surveyors engaged by Solas. It estimated that another €2 million would be required for the purchase of a site, giving an overall project cost of €6 million.
- 15.7** The business case also outlined proposals for how the project would be funded. This indicated that, in addition to a proposed €4 million grant from the Department, Solas had funding commitments from the Cultural Cinema Consortium (CCC)² for €750,000 and a further €600,000 from Galway City Council. As a result, the total projected public funding amounted to €5.35 million. The proposal indicated that the balance was to be acquired from a €400,000 commercial bank loan and private fundraising of €250,000.

¹ Solas is a company limited by guarantee with charitable status. Its members are representatives of the arts and film organisations in Galway City (Galway Film Society, Galway Film Fleadh, and Galway Arts Centre). The company went into liquidation on 3 July 2017.

² The Cultural Cinema Consortium was a strategic partnership between the Irish Film Board (IFB) and the Arts Council. Its activities were carried out between 2001 and 2010. The aim of the consortium was to enhance and expand the range of cinema in Ireland; to ensure audiences had access to a quality cultural experience with regard to world cinema, indigenous film-making and classic films; and to foster an attractive investment environment for art house film infrastructure.

- 15.8** The business case estimated annual cinema admissions of 64,100.¹ The projection was based on the 2006 census figures for Galway City, rural areas and satellite towns within the catchment area and a report —*Developing cultural cinema in Ireland*— published by the Arts Council. There is no evidence that sensitivity analysis of the project economics with respect to attendance rates was undertaken as part of the business case.
- 15.9** The cash flow projections for the project extended only to five years. In year zero, the projected capital costs were assumed to be matched by the various funding bodies and private equity. Trading income was expected to commence in year one and the project was projected to move into positive cash flows by year three.

Evaluation of grant application

- 15.10** The assessment of the applications under the ACCESS II scheme was carried out by an independent selection committee of four members which included a senior Department staff member, an Arts Council representative, a retired OPW architect and a retired Dublin City Council manager. The assessment methodology and terms of reference were determined by the selection committee.
- 15.11** The Solas application was initially assessed and recommended to proceed to a final evaluation. The final evaluation assigned specific marks in the following categories
- **local impact** — impact on other similar facilities in the relevant catchment area
 - **finance** — be in a position to achieve self-financing status into the future
 - **strategic compatibility** — be compatible with the national spatial strategy, or with objectives of other government policies, including the Arts Council's strategy, *Partnership for the Arts*
 - **need** — address a gap in provision, or address a proven need, within the relevant area
 - **design** — adhere to high standards in building design.
- 15.12** Following completion of the evaluation in March 2007, the selection committee recommended the project to the Department, proposing a grant allocation of €2.25 million. However, no evaluation was undertaken of the sufficiency of the funding requirements proposal.
- 15.13** The Department made a grant offer of €2 million, which was accepted by Solas in May 2007. As a condition of the grant, the Department required documentary proof to be submitted of both the full project costs and the availability of funds to meet those costs, before agreement was given to proceed to contract stage.
- 15.14** In addition to the Department's grant of €2 million, the CCC and the Irish Film Board (IFB) made funding commitments of €1.25 million and €400,000 respectively. Solas also secured a loan of €650,000 from the Western Development Commission (WDC).² By late 2007, the total committed and projected public investment in the cinema amounted to €6.3 million, including the purchase of a site by Galway City Council.

¹ Assumed scheduled weekly maximum capacity of 5,028 patrons for 51 weeks per annum, with utilisation (tickets sold) of 25%.

² The Western Development Commission was established on a statutory basis in 1999 to develop the western economy base (Donegal, Leitrim, Sligo, Mayo, Roscommon, Galway and Clare).

Site acquisition

- 15.15** Solas identified a site at Lower Merchants Road in the city centre as being suitable for development of the cinema. The company approached the property owner who, after negotiation, sold the property to Galway City Council in May 2008 for €1.8 million. Stamp duty amounted to €162,000, bringing the cost to €1.96 million. The City Council agreed to make it available for use by Solas under a 99 year lease.
- 15.16** Solas applied for and received planning permission from Galway City Council for a 360 seat cinema complex in 2008. This represented a 30% increase in capacity relative to the original proposal.
- 15.17** A new business plan was prepared by Solas in September 2008. This indicated the expected project costs increasing from the initial €6 million to €7.7 million. Additional financial support was sought from the Department.

First construction contract

- 15.18** In July 2009, following a tender competition, Solas awarded a contract to the lowest-cost tenderer to construct the cinema complex at a cost of €2.8 million. A contract guarantee bond for 25% of the contract sum (i.e. €696,000) was entered into by Solas with an insurance company.
- 15.19** Construction work, including a site survey, started on the site in October 2009. However, the project experienced significant difficulties over the next 17 months including
- initial severe weather conditions
 - unforeseen ground conditions, such as water ingress during excavation and unexpected granite bedrock
 - structural instability of adjacent property
 - insufficient project management in relation to the challenging site constraints.¹
- 15.20** Solas commissioned a second, more detailed ground survey, which identified more extensive challenges than the original site survey. By June 2010, it became evident that an adjoining property was unsafe and work ceased immediately. Following negotiations, Solas agreed to demolish and rebuild the adjoining property in October 2010.
- 15.21** The Department has stated that it understood two site surveys had been carried out on behalf of Solas in advance of the first tender competition in 2009.

¹ The issues were set out in a report in September 2012 by an architect engaged by the Department to represent its interests in the project.

Termination of construction contract

15.22 In March 2011, the Department received notification from Solas stating that the building contractor for the project was terminating the contract citing

- poor ground conditions
- design inadequacies and
- delays due to suspension of works while the builder was on site.

15.23 Solas submitted a claim under the bond arrangement in 2011. The bond became subject to a protracted legal dispute between the insurance company and Solas. In June 2017, Solas withdrew its claim in the Court of Appeal. In July 2017, Solas entered liquidation.

Second construction contract

15.24 Between 2011 and 2015, the development was marked by further delays and inactivity.

- A second construction contract was awarded by Solas in March 2012 for the remaining works. The Department has stated that this was done without its knowledge or consent. The Department received legal advice that it had no liability to release any further grant funds for the project.
- Under the second contract, the planned cost of construction increased from the first contract's €2.8 million to €4.1 million. This included demolition and reconstruction of the adjoining property at a cost of €213,000.
- The second contract was originally agreed as a single phase of building work. However, prior to commencement, Solas agreed with the builder to split the work into two separate phases. An analysis of the project budget by Solas in April 2012 had shown a shortfall in projected funding of over €1 million. Consequently, the company was in a position to fund only the initial phase of the work.

15.25 The first phase of work finished in early 2014. By July 2016, the project had not restarted and additional costs were identified relating to changes in specification, inflation and reopening of the site which had been closed for over two years. A private investor took over the management, completion and operation of the project and all Solas rights and liabilities transferred to it. The private investor was registered as the legal owner of a leasehold interest in the property in February 2017. Terms of the original lease were amended from 99 years to 30 years.

15.26 The new expected completion date is January 2018.

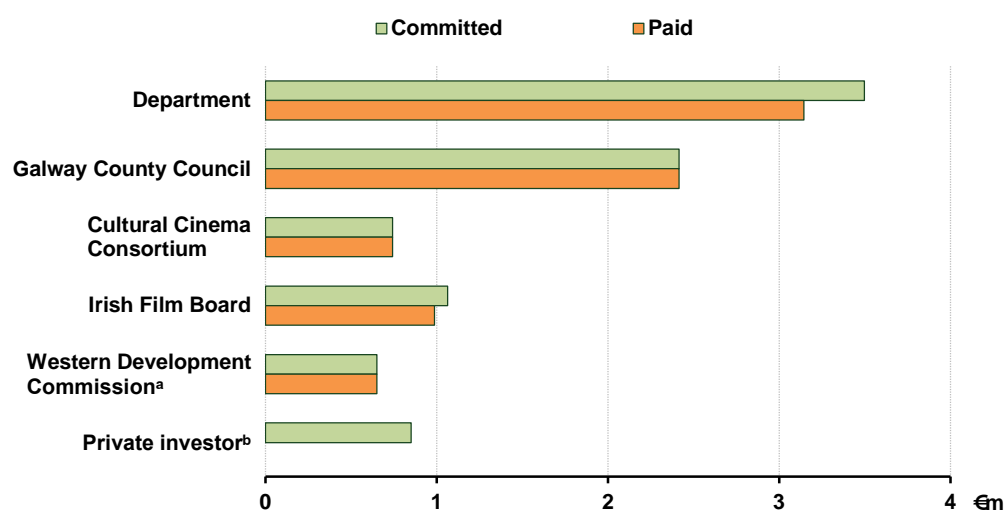
Company corporate governance

- 15.27** Over the period 2011 to 2014, the audited accounts of Solas indicated that the company was trading at a loss and its 2014 accounts reported an accumulated deficit of over €540,000.
- 15.28** The auditors of Solas resigned in October 2016 due to concerns regarding corporate governance in the company. Solas went into liquidation in July 2017.
- 15.29** The Department has stated that it was not notified of the auditors' concerns. It stated that it no longer has a funding relationship with Solas as the new investor has taken over all aspects of the project. It also stated that there is no incurred or potential loss of public funds as a result of the liquidation of Solas.
- 15.30** The Department had a legal charge on the property in the Minister's name since 2009. WDC and CCC/IFB registered charges on the property in 2009 and 2010 respectively in respect of their provision of funding. In late 2016, the Department revised its charge for the full amount of the grant already paid and the amount allocated and yet to be paid.

Additional funding commitments

- 15.31** The total financial commitments from public funds to the project have increased by €2.1 million since the initial funding allocations of €6.3 million in 2007. Figure 15.1 summarises the commitments.

Figure 15.1 Commitments and payments to Solas, 2007 to 2017



Source: Department of Culture, Heritage and the Gaeltacht

Notes: a Liability for the loan of €650,000 from the WDC transferred from Solas to the private investor in 2016.

b Details are not available on the amounts paid by the private investor.

- 15.32** In 2010, the Department took over CCC's remaining commitment of €507,500 arising from consolidation of capital funding within the Department and the Arts Council. The Department subsequently allocated additional funding of €990,000, comprising commitments of
- €735,000 in 2015, on condition that Galway City Council took over responsibility for managing the project to completion
 - €255,000 in 2016 to meet extra project costs.
- 15.33** The Irish Film Board increased its commitment from an initial €400,000 to over €1 million, comprising
- an additional €400,000 committed in 2013, in return for which Solas agreed to raise €500,000 in fundraising¹ and to secure €750,000 from a private investor²
 - additional funding of €263,000 in 2016 to meet extra project costs.
- 15.34** Galway City Council committed funding of €442,000 over the period 2013 to 2016.
- 15.35** The private investor committed €850,000 to the project. In addition, liability for the loan of €650,000 from the WDC transferred from Solas to the private investor in 2016. The loan is at a fixed rate of 1.45% for 20 years. WDC confirmed that the term loan was novated to the private investor and remains repayable on the same terms.
- 15.36** At August 2017, the Department has made payments totalling €3.14 million to the project and has remaining commitments to the project of €0.35 million. It stated that all payments are made on foot of invoices from the contractor in respect of work completed and are accompanied by a certificate from an auditor stating that the relevant work is actually completed and that the funds to pay for the work are not being recouped from any other public body.

Views of the Accounting Officer

- 15.37** The Department stated that it has at all times sought to ensure compliance with the terms and conditions of the grant scheme under which funding was awarded, and with public financial procedures generally. It stated that its involvement with Solas related to a capital grant for the construction of an art house cinema and it sought to ensure at each juncture that sufficient funds were in place to bring a completed cinema into public use. It stated that it had obtained documentary evidence for each strand of that funding and that there was ongoing monitoring of the continued availability of each strand of the funding.
- 15.38** The Department stated that when the project encountered significant difficulties in 2010 and 2011, it considered all possible options, including termination of the project. The decision to proceed was formally approved and involved serious consideration including risk analysis of the best approach most likely to deliver value for money for the taxpayer. The primary concern was the protection of the State's existing investment. In terms of providing funds, the Department's risk assessment was to continue supporting the project, or to cease support after the developer abandoned the project. The choice was between allowing the project to fail, whereupon the lease would revert to Galway City Council; or to facilitate an operator to enter negotiations with Solas to take over as project manager, leaseholder and operator. A further consideration was that the success of the project increased the likelihood of the repayment of the WDC loan as there was almost no prospect of its recoupment if the project was abandoned.

¹ Solas subsequently informed the Department that it was not in a position to raise the funds of €500,000.

² The private investment, which was secured in December 2013, was conditional on the granting to the investor of a long term lease to operate the cinema once complete.

- 15.39** The Department stated that it reviewed all possible options again in 2015 and 2016 and decided to continue funding the project.

Conclusions and recommendations

- 15.40** The Galway Art House Cinema project experienced significant delays and cost overruns since it was originally proposed in 2006. It was initially envisaged that the project would commence in 2007 and be completed in two years. The current expected completion date is January 2018.
- 15.41** The amount of public funds committed to the project increased by €2.1 million from the initial expected outlay of €6.3 million. The project has relied substantially on public investment to complete the development and to fund the increased project costs.
- 15.42** While the project was sponsored by a private entity with grant assistance from public funds, the State bore the financial risks which crystallised when the project ran into difficulties. A private investor took over the management, completion and operation of the cinema and has a 30 year lease on the property. Steps were taken through Galway City Council taking over responsibility for the project and the registering of charges on the property to safeguard the State's investment. There was no overall oversight arrangement in place for this project at the outset despite the involvement of a variety of public agencies.

Recommendation 15.1

The Department should review its approach to the projects which are being grant aided, in particular where the key project risks are carried by the State. Where projects do not progress as expected or serious shortcomings are identified with the project sponsor, early action needs to be taken, including formal reviews of the project viability, in line with the Department of Public Expenditure and Reform's *Public Spending Code* requirements.

Accounting Officer response

Agreed. The Department is fully committed to the ongoing management of projects in accordance with the *Public Spending Code* and relevant grant circulars. Measures are in place to ensure that staff are appropriately trained and supported in the appraisal and oversight of grant-aided projects as part of the Department's annual quality assurance process. The Department intends to hold further training sessions, accompanied by guidance material, prior to the end of 2017.

Recommendation 15.2

Particular care should be exercised by lead funders to ensure adequate formal oversight mechanisms are in place and operated where a variety of funding agencies are involved.

Accounting Officer response

Agreed. The Department will ensure that particular care is exercised in relation to the appraisal and oversight of projects in accordance with the provisions of the *Public Spending Code*. This will include further staff training on the early establishment of performance metrics to be used as a signal for action during the implementation phase, the need for regular management reports to be provided and reviewed, and dealing with project challenges.

Annex 15A Summary of events

2006	<ul style="list-style-type: none"> • Solas funding application in November 2006.
2007	<ul style="list-style-type: none"> • Solas application was assessed and approved by an independent selection committee. A grant offer was made by the Department and accepted by Solas in May 2007. The offer outlines the funding arrangement.
2008	<ul style="list-style-type: none"> • Solas received planning permission for the proposed development in May 2008.
2009	<ul style="list-style-type: none"> • In January 2009, the Solas board approved the architectural drawings for the final tender designs. These drawings provided for a 360 seat cinema complex. • A tender competition for a builder was launched by Solas in April 2009. Following evaluation of tenders received, a contract was signed by Solas and the builder in July 2009. • Construction started in October 2009. However, due to severe weather conditions, the project was initially delayed. • Ground excavation works caused structural problems for an adjoining property. Solas commissioned a second ground condition survey, which identified more extensive challenges than the original survey indicated.
2010	<ul style="list-style-type: none"> • Solas decides to cease work as the adjoining property was unsafe. • In October 2010, a plan to demolish and rebuild the adjoining property was developed and agreed by all parties.
2011	<ul style="list-style-type: none"> • In March 2011, the Department received notification from Solas stating the building contractor was terminating the contract citing: poor ground conditions, design inadequacies and suspension of works while on site. • Planning permission for the required demolition and rebuild of the adjoining building was obtained in April 2011.
2012	<ul style="list-style-type: none"> • A second tender to complete the project was undertaken and completed by Solas in March 2012. This was without the required knowledge or consent of the Department. • In early 2012, the Department was provided with legal advice that they had no liability to release any further funds to Solas to continue with the project. • The second contract was originally prepared as one phase. However, prior to commencement of works in early 2012, an agreement was reached between Solas and the new builder to split the works into two separate phases. The first phase was to complete the shell and the second phase involving the fitting out of the building.
2013	<ul style="list-style-type: none"> • In August 2013, Solas appointed an advisory group to engage in a consultative process to establish potential private funding options. • In December 2013, the Solas board presented their business plan to the Department and subsequently approved the heads of agreement with a private investor.
2014	<ul style="list-style-type: none"> • By early 2014, phase one of the works were substantially complete with the exception of some works which were omitted to facilitate phase two. However, due to insufficient funding, the second phase of the project did not proceed.
2015	<ul style="list-style-type: none"> • Galway City Council (Council) wrote to the Department confirming the Council was prepared to take over the project management and to make a further investment. However, this was subject to additional financial support from the Department. Despite the offer of significant additional funding, construction did not restart during 2015, due to ongoing difficulties between Solas and the second builder.
2016	<ul style="list-style-type: none"> • During 2016, the private investor took a more central role. Under this new agreement, all Solas rights and liabilities were assigned to the private investor. In parallel, the private investor engaged with the builder regarding the various obstacles to complete phase two i.e. fitting out the building. • In October 2016, the auditor of Solas resigned due to concerns regarding corporate governance in the company.
2017	<ul style="list-style-type: none"> • In July 2017, Solas went into liquidation. • Work on the cinema continues and the Department indicated an expected completion date of January 2018.