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THE CABINET

Thursday, 13th July, 2017 at 8.15 pm in the Conference Room, Civic Centre, Silver Street, Enfield, EN1 3XA

AGENDA – PART 1
TO FOLLOW PAPERS – 3RD DESPATCH

Please find attached a copy of the following report which was marked as "to follow" on the agenda previously circulated.

11. SMALL HOUSING SITES UPDATE (Pages 1 - 10)

A report from the Executive Director of Regeneration and Environment
Is attached. (Report No.24, agenda part two also refers) **(Key decision – reference number 4298)**

(Report No.21)
(8.45 – 8.50 pm)

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MUNICIPAL YEAR 2017/2018 REPORT NO. 21

MEETING TITLE AND DATE:
Cabinet – 13 July 2017
Council – 19 July 2017

REPORT OF:
Executive Director –
Regeneration & Environment.

Agenda – Part 1:	**KD 4298**
Subject: Small Housing Sites update. **Wards: Chase, Town and Turkey Street**	
Cabinet Member consulted: Cllr Oykener & Cllr Lemonides	

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1. EXECUTIVE SUMMARY

1.1 The Council entered into a Development Agreement (DA) in September 2014 with Kier to deliver 94 new homes over seven small sites. Kier had a separate JCT Design & Build Contract with Climate Energy Homes (CEH) who was named as the main subcontractor.

1.2 After entering into the DA, the Council established a wholly owned company, Enfield Innovations Ltd (EIL), in October 2014 to hold 57 of the 94 units as private rented homes. EIL took the benefit of the contract with Kier (jointly with the Council) and took responsibility for paying Kier (on Council approval) the original cost of the development in return for a 42 year leasehold interest in 57 of the 94 properties. The loan was to be repaid over 42 years using the income earned from renting the properties at market rents.

1.3 After site work had progressed CEH entered into administration in December 2015.

1.4 In order to continue the contract, Kier instructed Airey Miller Construction Management (AMCM) in December 2015 to audit the schemes and to support the completion of the homes as a Construction Management agreement.

1.5 Work continued within the original contract sum, until Cabinet approval could be obtained for any additional budget needed.

1.6 Due to the increasing costs caused by the combination of CEH going into administration and the nature of Construction Management agreements the Council sought independent cost advice from a cost consultant Mott MacDonald (MM). MM stated that the current projected cost of completing all the homes with Kier through the current contract did not represent value for money. Therefore alternative options have been considered.

1.7 Consequently this report seeks approval to terminate the agreement with Kier by negotiation of a fixed price contract, allowing them to complete three sites in total (noting they have already completed one site, St Georges) and to complete the agreed schemes at Parsonage Road and Tudor Crescent.

1.8 The procurement options for the completion of the four remaining sites at Holtwhites Hill, Jasper Close, Forty Hill and Lavender Hill are set out on Part 2 of this report.

2 RECOMMENDATIONS

2.1 Cabinet recommends to Council to approve the additional budget as set out in part 2 of this report to complete the two sites with Kier as set out in part 2 of this report and terminate the Development Agreement on terms including to complete Phase 1 for the additional sums set out in part 2 of this report.

2.2 Cabinet delegates authority to the Executive Director Regeneration and Environment and the Executive Director of Finance, Resources and Customer Services to conclude the details of the termination agreement referred to in 2.1 above. This will take into consideration the revised fixed price contract sum for partial completion of the Development Agreement in respect of completing 47 homes on three sites at St Georges, Parsonage Lane and Tudor Crescent only (Phase 1) as part of a negotiated commercial settlement.

2.3 Cabinet recommends to Council, subject to the Development Agreement being terminated with Kier, to approve the recommended procurement options as set out in Part 2 of this report for Phase 2 (Holtwhites Hill, Jasper Close, Forty Hill and Lavender Hill)

2.4 Cabinet recommends that Council approves the additional budget required for Phase 2, as set out on part 2 of this report.

3. BACKGROUND

3.1 In July 2012, Cabinet approved a sequence of reports (KD3517) for the clearance and redevelopment of seven 'Small Sites' and delegated authority to the Cabinet Members for Housing & Area Improvement and Finance & Property to appoint a development partner for all the sites. The original intention of the project was to develop the 57 homes for private sale to fund the 37 affordable homes.

3.2 Following a detailed competitive tender process, Kier Property Investments (KPI) was appointed to build 94 new homes, 57 for private rental (PRS) and 37 affordable units. The Development Agreement (DA) and S106 agreements were engrossed and leases completed in September 2014. The main subcontractor selected was Climate Energy Homes (CEH) and following vetting of their quality and capacity and following a Council visit to a Passivhaus project, it was agreed to appoint CEH.

3.3 The PRS proposal was put forward by Kier in their proposal. After due consideration of the successful bid, the Council agreed to adopt the PRS model and established a separate wholly owned Special Purchase Vehicle, Enfield Innovations Limited (EIL), in October 2014 to take a 42 year lease and provide the ongoing management of the 57 private rental units, rather than the short term sales approach originally envisaged.

3.4 Airey Miller Partnership acted as Project Managers (Employers Agent) for Kier under the JCT contract with CEH and provided reports and facilitated meetings between the Council and the Developers. It is important to note that the Council was not directly party to the JCT/CEH contract, but only had any relationship to any party through the DA.

3.5 Works commenced in December 2014. These were generally progressing well, up until the first properties at St Georges Road and Parsonage Lane were nearing completion, when CEH unexpectedly went into administration in December 2015. Kier were holding retentions and deferred payment sums at this point, which could still be reclaimed through a contractual challenge by Kier, but only upon completion of the administration process by CEH's administrators.

3.6 Kier appointed Airey Miller Construction Management (AMCM) to assess and fully audit the condition of the sites and consider delivery options. This audit was completed by April 2016.

3.7 AMCM identified that CEH had not completed certain works and had not undertaken some aspects of works correctly. This resulted in elements of remediation works being required before construction could progress. In addition, AMCM identified additional weather damage to structures despite the temporary weather proofing that was

put in place and its associated costs. Not only did work need to be rectified due to weather damage, but also components have had to be replaced through loss and damage as sub-contractors left the sites. Scaffolding was taken down which then had to be reinstalled once the contract was renegotiated.

3.8 After this period of due diligence in early 2016, the Council and Kier agreed that the best way to continue the project was to enter into a Construction Management Contract (CMC) with AMCM, as advice received was that tendering and appointing a new main subcontractor to continue on with what were substantially built structures would have proven even more costly and could have resulted in future liability and warranty issues. The other complication was that the Council were already committed to the timber frame system from Sweden (and sourced by Kier) that had been used by CEH, and is now integral to the scheme, therefore the CMC route offered the best solution to continue the works.

3.9 In summary, a CMC involves an item by item sub-contractor price with main contractor profit, but does not lead to a fixed price tender. The delay following the demise of CEH resulted in construction cost inflation taking effect, as all sub-contractors had to reprice the remaining work items.

3.10 AMCM were able to source the expertise and mobilise quickly enough and still provide the necessary warranties. This route did however mean directly tendering to main trades at market rates, which resulted in significant market rate increases. Since the appointment of AMCM, St.George's Road and Parsonage blocks A,B and C have been completed in November 2016, and 22 homes handed over.

3.11 In Autumn 2016, Kier advised the Council that there would be a significant increase in cost (when compared to the original contract sum) to complete the project. Due to the scale of this increase, the Council appointed independent cost consultants Mott MacDonald (MM) to test and compare the sums against recent tenders within Enfield and from their own database of similar recently tendered projects.

3.12 The contractual arrangements with Kier under the Development Agreement are such that they have limited liability of £2.2m for cost overruns, with contractual liability for any additional costs having to be met by the Council. Meanwhile the Council has been obliged to continue to pay Kier for their work, even if the cost is above the original DA contract sum. Progress on the contract has therefore been minimised until an agreed and revised budget can be approved by Cabinet. A practical solution had to be reached with Kier to disaggregate and terminate the current contract at an agreed point with fixed costs.

3.13 Officers met Kier in December 2016 to explain the concerns the Council had over the cost of continuing working via the Construction Management route and open discussions have progressed with Kier since then to agree a workable solution for both parties, through the disaggregation of the sites as the best way forward.

3.14 At Parsonage Lane, only block D remains to be completed and the houses at Tudor Crescent are significantly advanced and nearing completion, although the site also involves essential demolition of water damaged frames, which has been take account of within the proposed fixed price settlement. It is therefore recommended, due to the advanced nature of the sites, that it is prudent that Kier complete the construction on these sites only. Further negotiations on costs and recourse to retention and limited liability have also taken place with Kier as part of the proposed disaggregation and commercial settlement of the DA.

4. ALTERNATIVE OPTIONS CONSIDERED

4.1 *Immediate termination of the Kier contract without agreeing terms for Kier to complete Phase 1*. The Council could choose to terminate the whole agreement with Kier, but to do so the Council would have to claim that Kier were materially in breach of contract. As Kier have now passed the permitted extension of time, they are in breach of contract and we can terminate the DA. If we simply terminate without agreement this would mean that we have effectively six sites, in some cases part built, left to retender and complete, with all the delivery uncertainty that this entails. Kier have no wish to terminate the whole contract and the on site logistics and costs do not favour this approach.

Retendering <u>all</u> six remaining sites or partial sites to other developers/contractors. While this route may initially appear to produce overall construction cost savings, it has major drawbacks. Firstly, it would require the termination of the agreement with Kier in full, through a potentially protracted legal challenge. Secondly, it would involve decommissioning of Kier/AMCM's already on site presence and delay the programme still further while an alternative builder was procured. Thirdly, we have no certainty that other contractors would be willing to take on the obligations and warranties of the contract, or in fact provide a financially viable contract price, resulting in even further delays and contract uncertainty.

4.2 The structure of the DA is such that the Council's ability to pursue Liquidated and Ascertained Damages (LADs) for delay only arises once the extended longstop date is reached and the agreement has not been fulfilled; a position reached at the end of January 2017. LADs recoverable are relatively small in comparison to the overall increased costs. Kier have been notified of the Council's intention to claim LADs

from January 2017, and these have been taken account of in the proposed settlement.

4.3 *Continue with Kier for Phases 1 & 2*. The continuation of the current agreement in its entirety with Kier would leave the Council exposed to costs over those anticipated through the route recommended in this report. This being the assessed position, is not therefore a recommended option.

4.4 *Sell the sites incomplete*. All remaining sites have detailed planning approvals. Consequently, disposing of the sites on the open market represents an option to mitigate further costs. However, planning requirements for affordable housing provision are structured across all of the sites and so would require renegotiation by any prospective site purchasers, thus impinging on value. Disposal of the sites would lose the benefit of the complete assets (new homes) to the Council, both in terms of the capital value of the asset and the notional financial value of reducing the costs of affordable and temporary accommodation currently paid.

4.5 Having considered the financial implications of the various options described above, they were discounted on the basis that they could not achieve a financially viable scheme and resulted in significant further losses to the Council.

5. REASONS FOR RECOMMENDATIONS

5.1 The Council faces significant additional costs both to continue under the current agreement to conclude the full contract with Kier or through the alternative options that have been considered. The most cost effective way for the Council to conclude this contract is to complete the two sites with Kier under the terms of the settlement agreement and agree a fixed price contract with AMCM to complete the remaining four sites. This approach will enable the best financial outcome for the Council in the circumstances and result in a financially viable scheme which retains the original proposed affordable housing element.

5.2 As work being undertaken by Kier is almost complete at Parsonage Lane and significantly advanced at Tudor Crescent, continuation with Kier for Phase 1 until completion represents the most expedient way forward to mitigate and minimise the Council's significant financial exposure. It is unlikely that another contractor would take on the design responsibility and component indemnity for work done by another party and external advice has indicated it is likely to be more expensive if they did.

5.3 There was the possibility that Kier may have challenged any attempt to withdraw from the agreement before full completion on the basis of loss of profit, and equally the Council had the right of levying LADs, and challenging works undertaken to date. We have now established a

foundation for a negotiated and amicable commercial settlement if the two sides can agree a 'cancelling out' of claim and counter claim and save protracted and significant legal costs. All parties are now committed to agreeing a negotiated settlement and completing the scheme.

5.4 The principle of contract disaggregation was agreed with Kier at the end of December 2016. Kier have subsequently continued to maintain responsibility for the sites, with minimal works progressing until a Cabinet approval could be obtained; however, they have stated that they cannot continue working any further above the original contract sum without formal approval by the Council for the proposed settlement as set out in this report. There is a therefore a significant risk that works could be halted altogether by Kier, resulting in a legal confrontation, creating further complications of potential weather damage, cost and delays if a Council decision to the disaggregation contract cannot be approved and concluded.

5.5 MM have now completed a full audit of sites works, and contract costs to date from Kier and have fully substantiated all payments authorised by the Council to date. They have also undertaken an evaluation of additional costs to conclude the proposed disaggregation (Phase 1) contract, and Phase 2, details of which are set out in part 2 of this report. The tender report produced supports that the fixed price completion costs represent value for money, considering the contractual issues, constraints and complexities of the project.

5.6 MM have also undertaken an audit of the timber frame panel system, which is currently in secure storage in London awaiting delivery and erection. As the Council has paid for the panels and continues to pay for their storage, it is essential that the storage conditions and frames themselves have been checked to provide assurance as they continue to be stored prior to construction.

6. COMMENTS OF THE DIRECTOR OF FINANCE, RESOURCES AND CUSTOMER SERVICES, AND OTHER DEPARTMENTS

6.1 Financial Implications

6.1.1 A significant amount of financial modelling of alternative options was undertaken prior to identifying the preferred route to move forward with this project. The options explored included variants on the delivery of the contract and variants relating to the eventual tenure of the 94 properties to be delivered.

6.1.2 The overall viability of the scheme was considered, as well as the financial impacts on the Council's Housing Revenue Account and General Fund, and Enfield Innovations Ltd (EIL). The option proposed is financially viable and is the most the most financially beneficial and

deliverable for the Council and EIL, and allows the Council to deliver the 37 affordable homes as originally proposed.

6.1.3 Provision can and will be made in the appropriate budgets to allow the Housing Small sites project to conclude.

6.1.4 Further, more detailed, financial implications are contained in Part 2 of this report.

6.2 Legal Implications

See Part 2 report

6.3 Property Implications

6.3.1 It is recommended that any future payments made to Kier are captured in appropriate legal contracts which will ensure that any overrun of costs sits with Kier. The liabilities clause with Kier should adhere to the Council Contract procedure rules, where practicable, taking into account that this is a proposed termination of the DA, rather than a new construction contract.

7. KEY RISKS

7.1 If the recommendations are not accepted, the project will be delayed still further, resulting in the risk of significant higher costs and liability for the Council, through legal challenge and seeking alternative and more challenging procurement options to conclude the scheme.

7.2 If the recommendations are not accepted then the part finished properties and works are likely to deteriorate in condition further leading to further losses.

7.3 Procurement risks – As set out in Legal Implications in Part 2.

7.4 Reputation – One of the key objectives of the project was to provide Affordable Homes, part funded by the private rented homes. The proposed recommendations in this report ensure the Affordable Housing can still be provided and a long term financially viable scheme delivered. If the recommendations are not accepted, then there is a significant risk the project cannot continue, therefore achieving no affordable homes. Any properties already completed would have to be sold, however they would not cover the current scheme financial outlay.

8. IMPACT ON COUNCIL PRIORITIES

8.1 Fairness for All

The Small Sites project contributes to this aim by tackling inequality and access to social housing by providing new homes, a mix of tenure and employment opportunities across the area.

8.2 Growth and Sustainability

The Small Sites project contributes to this priority by building strong and sustainable futures for our residents. The scheme attracts investment from the private sector, promotes off site building that is environmentally friendly and prioritises environmental sustainability including improving the energy efficiency of the residential buildings.

8.3 Strong Communities

Direct involvement in the process has allowed local people to shape the plans and fostered a greater sense of community cohesion.

9. EQUALITY IMPACT IMPLICATIONS

9.1 The overall scheme has been subject to an EIA.

10. PERFORMANCE MANAGEMENT IMPLICATIONS

None

11. HEALTH AND SAFETY IMPLICATIONS

None

12. HR IMPLICATIONS

None

13 PUBLIC HEALTH IMPLICATIONS

13.1 Housing is a determinant of health and this proposal should therefore positively impact the health of prospective residents. All of the homes will be designed to achieve or exceed the Mayor's internal space standards, amenity space standards, and achieve high levels of sustainability and energy efficiency.

Background Papers
None

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