

Bronzeoak - Budget

Housing Committee Tuesday, 23 January 2024

Report: Director of Resources (S151)

Purpose: For decision

Publication status: Unrestricted

Wards affected: Valley

Executive summary:

The Council's redevelopment of Bronzeoak House, to provide 26 new homes for affordable rent, has been inactive since the financial failure of the main contractor in May 2023. This report:

- Provides an update on work being done to restart construction works
 - Provides an overview of the project's financial position to date
 - Seeks additional budget for completion of the work
 - Seeks authority to complete the works by entering into a construction management contract with the contractor
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This report supports the Council's priority of: Building a better Council/
Creating the homes, infrastructure and environment we need

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Recommendations to Committee:

That:

- A. The Committee approve the appointment of a construction management contractor to facilitate the completion of the Bronzeoak House development in Caterham.
- B. Authority be delegated to the Director of Resources, in consultation with the Chairman and Vice Chairman of the Housing Committee, to award the contract to the contractor, Cast & Teller Limited, following completion of due diligence and a value for money report from the Council's employer's agent.
- C. The Committee approve the increase in project budget from £10.6m to £13.2m

Reason for recommendation:

To seek Committee approval to progress the Bronzeoak scheme and increase the budget, following the administration of the original contractor, Claritas Group Ltd.

Introduction and background

- 1.0 The Council purchased Bronzeoak House in May 2018 for the sum of £2.2m.
- 1.1 In December 2019, the Council gained planning consent to construct 26 new homes for affordable rent, in the form of 12 x 2 bed flats for general needs and 14 x 1 bed flats for sheltered housing, to assist with meeting the demand from the housing register and to improve the Council's supply of sheltered accommodation in line with its Housing Strategy.
- 1.2 Following a competitive tender exercise a 'design and build' contract was awarded to Claritas Group Ltd and the contractor took possession of the site in October 2020. The project was forecast to complete in the summer of 2022.
- 1.3 The project has been negatively impacted by a series of national and world events including Brexit, the Covid pandemic, the war in Ukraine and the rise in inflation.
- 1.4 Claritas Group Ltd experienced significant cash flow issues because of the above market forces and entered administration in May 2023 owing creditors in excess of £8m.

- 1.5 In August 2023, the Council appointed a construction management company ('CMC') to engage with the former sub-contractors and establish the most cost effective and efficient return to complete their works. This arrangement would involve the Council paying the former sub-contractors directly and would allow the Council the benefit of their original obligations with regards to design, guarantees or warranties for their works.
- 1.6 As part of the procurement process, a cost report was produced which concluded that continuation of the work by the former sub-contractors will cost circa £3.2m (this is based on existing contract sums but also includes a contribution from the Council towards 'aged debt'). In contrast, a full procurement of the individual works contracts with a new supply chain has been estimated at circa £3.5m. This estimate is under review by the Council's employer's agent to confirm it is a fair and accurate reflection of costs in the current market. Whilst it is not incumbent on the Council to meet the debts of the previous contractor, if doing so secures the services of the existing sub-contractors and allows the project to be completed more quickly and at a lower cost, then it is financially pragmatic to do so. As set out below, this approach will also allow for the retention of warranties and accountability for work partially completed by sub-contractors.

Construction Management Contract

- 2.0 The JCT Construction Management Contract is for use on construction projects where the Employer (the Council) appoints separate trade contractors to carry out the works, and a construction manager is appointed to oversee the completion of the works for a fee.
- 2.1 The construction manager will be appointed to manage and supervise the project, act as 'Principal Contractor', act as an agent on the Council's behalf by issuing instructions, making decisions and preparing certificates. The construction manager should have the skill, experience and relationship to co-ordinate and cajole the other contractors to progress the works to completion.
- 2.2 A CMC is often used where there is separate contractual responsibility for the design, management and construction of the project. Given the complexities of the build at Bronzeoak and the absence of the previous 'main contractor' there is a significant benefit to the Council in maintaining continuation of prior works' responsibility, warranty and knowledge of the project by negotiating with and directly appointing the sub-contractors to continue. This approach will also allow for a more expedient re-start of works with minimal mobilisation and start up time.
- 2.3 Under a CMC, the Council would retain the services of its employers agent to advise and act on behalf of the Council. The Council would also retain the services of its clerk of works to carry out independent weekly inspections of the construction works.

Budget

- 3.0 A budget of £9.695m for the redevelopment of Bronzeoak House was approved by this Committee in September 2019.
- 3.1 The subsequent tender process saw tenders received which were all more than the forecast cost of works and as a result the budget was increased to £10.6m by this Committee in June 2020.
- 3.2 To assist Claritas Group Limited with reported cash flow issues a financial support package was agreed by this Committee in November 2022 and the Council entered into a performance-incentivised Settlement Agreement.
- 3.3 In order to assist with cash flow, some additional payments were made by the Council direct to sub-contractors for work done in the period leading up to Claritas going into administration. Unfortunately, it quickly became apparent that the company would not be able to recover its financial position. Claritas Group Ltd were unable to achieve any of the required milestones to trigger additional direct payments to them under the Settlement Agreement. The Settlement Agreement was a bespoke agreement with Claritas to deal with a specific situation and as such the approved budget remains at £10.6m.
- 3.4 The cost of the construction project so far (including acquisition, demolition, planning and design fees) is approximately £9.6m.
- 3.5 The proposed cost to complete, under a CMC is forecast to be c.£3.2m (including the CMC fee of 6.5%) bringing the forecast total cost of the project to £12.8m.
- 3.6 In order to complete the construction of Bronzeoak House, Officers therefore recommend that the previously approved budget of £10.6m be increased to £13,200,000. This includes a contingency.
- 3.7 The Council has a Performance Bond which it intends to claim against in full, equal to £772,632. The performance bond is not paid until after completion of the project. This could reduce the total cost of the project to £12.4m.
- 3.8 Site security is currently costing £22,000 per month and the loss of rental income is approximately £21,000 per month.
- 3.9 Bronzeoak House is already over the original budget that was forecast at the time of acquisition and is likely to be the most expensive housing redevelopment scheme. However, the scheme is one aspect of the wider Council house building programme which, whilst being one of the Council's objectives, does carry considerable risk. Some schemes will always perform better than others and Members are assured that the overall programme can withstand the costs associated with the completion of Bronzeoak House, even more so now that the Council has Investment Partner status and is in receipt of Homes England grant on schemes that were modelled and approved without it. £1.5m of funding has been received to-date for schemes that were intended to be funded through borrowing.

Other options considered

- 4.0 Instead of using a CMC, the Council could adopt the same approach to re-procure as it has taken at Uplands in Warlingham. This would involve re-tendering for a new main contractor who will subsequently tender the remaining works to other sub-contractors. However, Uplands was much closer to completion when W Stirland went into administration, was a more traditional and less complex building and had the benefit of having collateral warranties in place for works completed. Notwithstanding the above, Uplands has continued to suffer problems associated with one contractor endeavouring to complete another's work. In the case of Bronzeoak, the Council's employer's agent has advised that the use of a CMC would be the most appropriate route to completion.
- 4.1 The benefit of a CMC at Bronzeoak is that continuation of works would be based upon using known sub-contractors, benefitting from their detailed knowledge of the project and assuming responsibility of their prior works, including where collateral warranties have been agreed but works are incomplete. It would be difficult and expensive to employ a new sub-contractor to complete the detailed design of another and highly unlikely that any new contractor will provide a warranty for work they have not done.
- 4.2 An example of one of the many issues at Bronzeoak is that the lifts have been installed by Kone - but not yet commissioned. The Council will not find another lift contractor who would be willing to commission and certify Kone lifts. The Council has paid for the lifts in full but Kone did not receive the payment from Claritas. Kone are demanding full payment of the lifts before they will return and do the commissioning. It is still more cost effective for the Council to pay Kone twice for the lifts than to source a new lift contractor to start from the beginning.
- 4.2 The CMC, acting as a consultant, has been in negotiations with some of the suppliers and contractors at Bronzeoak and the majority have indicated their preparedness to return and complete their work. The Council's contribution towards money owed to them by Claritas i.e., 'aged debt' to facilitate their return is still the most cost-effective way of completing the project. Where this is not the case the Council will instead seek to re-procure, if necessary.
- 4.3 The current financial modelling for Bronzeoak is based on levying an affordable rent at 70% of the Open Market Rent (OMR). It remains an option for the Council to charge 80% of OMR. This would improve the financial performance of the scheme but the units would be less affordable to persons on the Council's housing register.
- 4.4 The Council has commuted sums available of just over £800k which it could use to fund the increased costs of the Bronzeoak House project. This would improve the performance of the scheme but will mean that the commuted sums would not be available to grant fund new home delivery via a housing association or provide additionality on other schemes.

- 4.5 The above two paragraphs are for information and discussion and to make Members aware that these options are being considered. It is not necessary for Officers or Members to decide on either at this stage. An update will be provided to Members at a later committee once Officers have more cost certainty. This will allow Members to take a more informed decision should the above recommendations be put forward at that time.
- 4.6 Officers have considered whether it is appropriate to apply for Homes England grant to assist with the costs of delivering the Bronzeoak House scheme. However, 40% of the scheme costs so far have been funded by Right to Buy receipts and it is not permitted to use both RTB receipts and HE grant in the same unit. The process of splitting funding out between some grant funded units and some RTB funded units would be incredibly complex, given that the development is a block of apartments with shared facilities. Furthermore, and more crucially, Homes England would need to be satisfied that the use of grant in this case would represent good value for money and Officers would not be able to successfully argue this point, given the costs that have been incurred to date on the project.**Summary**
- 5.0 The development of Bronzeoak House has been a significant challenge, both in terms of detailed design and finance. However, its delivery will assist the Council in meeting one of its main priorities in that it will deliver 26 new affordable homes for individuals waiting to be rehoused on the Council's housing register. In addition to 12 flats for general needs, 14 of the homes will be new sheltered housing, allowing the Council to re-house existing and new sheltered housing residents in well-insulated, accessible and modern homes in a sustainable location. The provision of sheltered housing in this location has facilitated the pipeline schemes at Pelham House, Stanstead Road and Kentwyns, creating more opportunities for new affordable homes. Prior to the Council's acquisition, Bronzeoak House was a vacant building that was unattractive and the site of considerable anti-social behaviour. The original planning approval would have delivered 34 one-bed flats for market sale which may well have been profitable for a private developer but would have contributed substantially less to the District in terms of social value.

Key implications

Comments of the Chief Finance Officer

The financial impact of the recommendations and the history of the scheme are set out in the body of the report, which is focussed on financial aspects of the project.

The scheme is funded from the HRA, which is ringfenced for the provision and management of council housing. Whilst the recommendations therefore have no General Fund financial impact, it is nonetheless important for the Council to make the best overall decision, balancing the need to provide council housing and complete a significant part of the overall programme against the need to provide value for money.

There are no obviously viable alternatives but to complete this scheme and, subject to further due diligence, the option proposed offers the best overall value for money.

Comments of the Head of Legal Services

Design & Build has been the most common form of construction contract for large scale projects and has been previously used in majority of the Council schemes. This enables design and construction activities to overlap benefitting programme and transfers much of the delivery risk to the contractor for a fixed price and an agreed programme. As stated in this report, the Council has an option to consider entering into a JCT Construction Management Contract in order to complete the redevelopment scheme on the Bronzeoak site. Should Members be mindful to agree to proceed, the appointed CMC would not be required to carry out any construction works but instead be paid a fee to manage the construction works carried out by others. The CMC in effect would provide services and not works. Risks will need to be managed throughout this redevelopment process and a risk register should be in place with appropriate mitigation identified.

Equality

See original report

Climate change

See original report

Appendices

None

Background papers

None

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