



Mayor and Cabinet

Home Park and Edward Street Developments.

Date: 19th July 2023

Key decision: Yes

Two-part report:

Part 1: Summary, Recommendations, Background, Risk and Disposal Options

Ward(s) affected: Deptford and Bellingham

Outline and recommendations

1. Mayor and Cabinet are asked to note:
 - a) The background to this contract with a total scheme cost of £34m to invest in modular homes on the Home Park and Edward Street sites, split £13.5m and £20.5m respectively with the delivery of the development tasked to Lewisham Homes.
 - b) The intended outcome to bring forward 31 social homes on the Home Park site within the HRA and 34 social/temporary accommodation homes on the Edward Street site within the General Fund.
 - c) That the appointed contractor, very late in the offsite construction and site preparation phases, has gone into administration leaving the commissioned units incomplete and not meeting the contracted specifications.
 - d) Following the company's collapse into administration, the extensive work undertaken to explore options for continuing the schemes or mitigating the loss the Council from aborting them.
2. Mayor and Cabinet are asked to approve the recommendation for Officers to progress Option 1 as set out in this report with the commercially sensitive and confidential aspects covered in the part 2 report on the agenda.
3. Mayor and Cabinet are also asked to approve the delegation to the interim Executive Director for Place, in consultation with the Monitoring Officer and s151 Officer, to work with Lewisham Homes to implement Option 1.

Timeline of engagement and decision-making

Mayor and Cabinet, 11 July 2018 - New Homes Programme

Mayor and Cabinet, 10 October 2018 - PMH Programme Update & Procurement Strategy

Mayor and Cabinet, 15 January 2020 - Building for Lewisham Programme

Mayor and Cabinet, 11 March 2020 – Precision Manufactured Homes Programme Procurement Part 2

Mayor and Cabinet, 8 July 2020 - Building for Lewisham Update

Mayor and Cabinet 6 July 2022 – Edward Street and Home Park Update report

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1. Summary

- 1.1 Following the launch of the Building for Lewisham (BfL) programme in January 2020 and building on the previous New Homes Programme, Lewisham Homes were the Council's direct delivery partner building new Council homes.
- 1.2 It should be noted since March 2023 this programme is now being delivered in house through the Council direct delivery team.
- 1.3 The BfL programme adopted a mixture of construction methods to deliver the new homes. Most of the programme being delivered through traditional building methods, however following the success of the PLACE Ladywell project, two projects in the programme were identified to be delivered through modern methods of construction (MMC), namely homes being built in a factory and then transported and assembled on site. The projects are at Home Park in Lower Sydenham and Edward Street in Deptford.
- 1.4 Following a competitive process, Caledonian Modular Ltd (CML) were selected as the main contractor for both projects.
- 1.5 Lewisham Homes entered contract with CML in August 2020 for a contract value across both sites of circa £25m. Work commenced on building the modules in the CML factory as well as works on the individual sites to prepare them for the delivery and ultimate assembling of the modules.
- 1.6 In March 2022, the Council were informed that CML had entered administration. Remaining amounts across both projects totalled circa £10m remaining.
- 1.7 Lewisham Homes own and have vesting certificates for the partially completed homes. These are currently being stored offsite.
- 1.8 Since then, officers have been reviewing options for these projects and this report sets out the options considered, risk and financial implications.
- 1.9 Following CML insolvency and the integration of Lewisham Homes development team into the Council it has been agreed that the ongoing management, oversight, decisions required, and risk should be managed by the Council as shareholder of Lewisham Homes.
- 1.10 It should also be noted that any cost recovery through ongoing legal claims and potential disposal of assets with any value obtained is paid directly to Lewisham Homes to offset any ascertained losses.
- 1.11 Following analysis of the options available the recommendations support that they are removed from the capital programme and priority is given to cost recovery through all routes available.
- 1.13 Following contractor insolvency Lewisham Homes secured the sites, completed the relevant legal notices and began activation of the performance bond within the contract.
- 1.14 The performance bond being a surety bond and mechanism contractually for the employer to recoup fixed costs for non-completion of the contract. This sum is capped at 10% of construction cost across both projects therefore will not cover majority of spend to date.

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Options for the partially completed homes outlined within this report:

- i) Disposing of the modular homes for best value, assessing other options for the two sites and focusing on cost recovery.
- ii) Completing the works with newly owned company JRL Group
- iii) Completing the works through competitive market tender

We will outline within this report the risk attached to each option above and therefore our recommendation for members on both sites.

2. Recommendations

2.1 Mayor and Cabinet are asked to note:

- i) The background to this contract with a total scheme cost of £34m to invest in modular homes on the Home Park and Edward Street sites, split £13.5m and £20.5m respectively with the delivery of the development tasked to Lewisham Homes.
- ii) The intended outcome to bring forward 31 social homes on the Home Park site within the HRA and 34 social/temporary accommodation homes on the Edward Street site within the General Fund.
- iii) That the appointed contractor, very late in the offsite construction and site preparation phases, has gone into administration leaving the commissioned units incomplete and not meeting the contracted specifications.
- iv) Following the company's collapse into administration, the extensive work undertaken to explore options for continuing the schemes or mitigating the loss the Council from aborting them.

2.2 Mayor and Cabinet are asked to approve the recommendation for Officers to progress Option 1 as set out in this report with the commercially sensitive and confidential aspects covered in the part 2 report on the agenda.

2.3 Mayor and Cabinet are also asked to approve the delegation to the interim Executive Director for Place, in consultation with the Monitoring Officer and s151 Officer, to work with Lewisham Homes to implement Option 1.

3. Background

3.1 Actions and negotiations since administration

3.1.1 It should be noted that contractor insolvency is impacting all organisations across the sector and as an example, recent government statistics show there were over 2,000 company insolvencies in March 2023 – a 16% rise on the same month in 2022. This data also shows construction as the hardest-hit sector for company insolvencies in the UK this can be down to several reasons including high inflation and interest rates.

3.1.2 We have also seen a rise in negative attention within the press impacting the modular

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homes construction. Ilke Homes closing operations, Legal and General significantly reducing activities and some Caledonian Modular completed developments being highlighted in press due to quality issues. These issues are wide and far reaching with ramifications impacting several organisations across the sector.

- 3.1.3 This sharp rise in insolvencies is down to many factors which include long term effects of the pandemic, the Russian/Ukraine conflict, overall inflation, and the increase in energy prices.
- 3.1.4 The schemes at Home Park and Edward Street are Precision Manufactured Homes (PMH). These are homes that are built offsite in a factory and then delivered to the site for assembling and final fix of services. PMH is considered a form of Modern Methods of Construction (MMC).
- 3.1.5 The Council has been at the forefront of PMH homes in the sector having delivered the award-winning PLACE Ladywell building in 2016. The building provides 24 x two-bedroom temporary homes and commercial space.

The schemes at Home Park and Edward Street were identified as part of the Council's legacy of providing good quality PMH homes. Whilst the Council has experience in providing PMH homes, the use of PMH to deliver affordable housing is still relatively new within the sector.

- 3.1.6 Modular construction comes with many efficiencies coupled with a degree of risk. Some of these include speed of delivery, energy efficient homes, safety during construction and quality management. However, this method of construction does carry risks and these risks have been seen and experienced by many developers in both the public and private sector over many years.
- 3.1.7 The main risk attached to this form of construction is contractor insolvency during construction which we have seen across both sites. When this does happen, it can be very difficult for Clients to secure the product and continue to delivery. This coupled with a rise in build costs not seen in some decades makes delivery challenging.
- 3.1.8 Early in the contract there had been some unexpected delays and costs to both schemes which resulted in delays to the programmes. Officers were preparing to present a report to Mayor and Cabinet in March 2022 referencing these when we were informed that CML had entered administration.
- 3.1.9 The report was withdrawn whilst officers considered the impact of the administration and explored the options for the future of the projects.
- 3.1.10 Following CML administration, Lewisham Homes acted quickly to secure the sites and the homes and undertook several activities – including, completing the necessary cable diversions and undertaking temporary drainage works on Home Park, instructing a full condition survey of the modules for both sites, adapting hoardings to allow for temporary traffic management equipment to be removed and ensuring that both sites were set up with remote security monitoring.
- 3.1.11 The project team also identified that a component of the construction did not comply with our own employer requirements specification. This issue related to the vapour control layer “VCL”. A VCL is a component mainly designed to protect the property from condensation, mould, and damp. The products used were A2 rated however within our specification we require A1 rated.

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3.1.12 Therefore, if the properties were built to completion remediation would have been required. The cost of this remediation is included within our cost estimates to date. If these homes are ultimately disposed of, any value reduction due to the VCL specification will be part of a claim to the Caledonian Modular professional indemnity policy. This is being managed by the commissioned legal advisors for the scheme.

3.1.13 On 1 April 2022, the JRL Group purchased the assets of CML but not the business. This created a 'phoenix company' which is known as JRL Caledonian. These assets do not include the completed modules which are owned by Lewisham Homes/Council.

3.2 JRL Negotiation

3.2.1 Given the investment to date the focus and priority of the project team has always been to complete remaining works and deliver the housing planned for both sites. Therefore, work was undertaken by JRL Ltd to provide a costed PCSA scope for both sites, to include module remediation and design works. This was followed by a main works contract cost for the installation of modules on site and completion of the onsite works. Neither the PCSA nor the contract was entered into due to higher-than-expected cost estimates and tender prices received.

3.2.2 Simultaneously to JRL providing cost estimates our appointed QS team at Arcadis provided independent cost advice on their own assessment of costs to complete

3.2.3 The works cost tenders and estimations provided by both JRL and Arcadis heavily exceed the amounts remaining within the Caledonian modular contracts by significant sums and therefore create an unviable position on both sites.

3.2.4 In summary both development options will require a c30m additional investment to deliver these sites in the current form with the usual development risk.

3.2.5 Therefore, exit and delivery options have been considered across both sites.

3.3 Disparity between remaining contract sum and estimated cost to complete:

3.3.1 Lewisham Homes entered contract with Caledonian Modular mid-2020. Since this time, we have seen unusual and significant industry events which have impacted a rise in build costs across the sector. Rising works costs comprise of general inflation, labour costs and materials all increasing at a higher rate than experienced in decades. The rise in build costs is a significant factor influencing the high works costs estimated and tenders received by JRL and Arcadis.

3.3.2 Due to the estimates received to complete the works the following three options have been reviewed:

- i) **Option 1:** Do not proceed with works. Abort project in current form with costs. Establish a new use for the site and maximise cost recovery.
- ii) **Option 2:** Carry out remaining works on site. Continue to negotiate with JRL at an indicative cost identified.
- iii) **Option 3:** Carry out remaining works on site. Procure and carry out remaining works with a suitable contractor yet to be identified.

3.3.3 All the above options will carry political, economic, social, legal and environmental risk.

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- 3.3.4 Priority will be to deliver best economic and social value for the council and residents.
- 3.3.5 Summaries and financial details of each option will be contained in part 2 of this report.

Option 1 – Do not proceed with works. Abort project in current form with costs, as per costs identified within Part 2 report

Mitigation and cost recovery

Performance Bond: Claim underway

PI insurance claim: Lewisham Homes' legal team have advised that Lewisham Homes have a potential PI claim due to specification breach on both sites. We are yet to establish an indicative amount with the legal team for this at present and will also be dependent on future use of the pods.

Value of pods in current form. We have instructed JLL to carry out a valuation of both the existing use value, demand in market and land value and option analysis. This piece of work is expected July 2023 and will inform our next disposal options.

GLA grant on Home Park has been repaid.

GLA grant on Edward Street to be repaid if decision taken not to proceed.

Option 2 – Proceed with works on site. Continue to negotiate with JRL, as per costs identified within Part 2 report

Option 3 – Proceed with works on site. Establish procurement process for preferred contractor, as per costs identified within Part 2 Report.

3.4 Risk

- 3.4.1 **Financial impact** – All three options carry significant financial risk. If the Council were to decide to abort the current scheme through option 1, it must maximise its potential returns through insurance claims and potential disposal of the units and land value obtained.
- 3.4.2 **New contractor premium:** If the Council were to decide to pursue delivery through option 2 or 3 and carry out the works, the work on both sites will come at a premium and will impact the viability of both schemes. The perceived risk that an incoming contractor will need to accept will influence cost. This has been evidenced in both Arcadis' independent cost estimate and the JRL contractor price estimate.
- 3.4.3 **Programme** – the selection and appointment of a new contractor plus the works on site and the remedial work to the modules will undoubtedly result in programme delay. If the Council were to decide to re-procure the sites within the market, it would have no guarantee of an active market at the likely point of procurement.
- 3.4.4 **Rising works costs:** Impact of inflation, labour, materials and uncertain market – it is difficult to predict how the cost to complete works will be affected by construction inflation given the levels of market uncertainty – however cost advice from Arcadis has indicated

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a likely significant premium, higher the value of the previous works contract with Caledonian Modular.

3.5 Storage and security costs for modular homes

- 3.5.1 Since the pausing of negotiation with JRL they have advised storage costs will now be payable from March 2023 and up until present.
- 3.5.2 JRL have advised of these costs and there are identified within Part 2 of this report. These costs relate to site security and storage. To transfer these units to another site would require significant space and capability to store such a significant number of modular homes. The Council would also incur a significant cost to move the pods and to co-ordinate and incur future security costs.
- 3.5.3 It is acknowledged the ongoing storage costs are high, however given the significant investment to date it is important all options have been considered and assessed before proceeding to disposal. This work has been undertaken by the project team and appointed consultants and advisors. Therefore, this report recommends a decision to accelerate disposal of these units once approved by cabinet.

3.6 Recommendation for cabinet and supported by Officer New Homes Programme Board in May 2023:

- 3.6.1 Given the significant capital investment to date on the units, the high estimates to complete the works and the further risks associated, it is recommended that option 1 is preferred and no further costs are incurred.
- 3.6.2 If this option is supported by Mayor and Cabinet, officers will continue to prioritise cost recovery through our legal claims and disposal of the partially completed homes.

3.7 Disposal options and next steps:

- 3.7.1 Subject to the approval of Mayor and Cabinet, work to progress the disposal of the homes will proceed in the second half of 2023. The options for disposal will include:
- 3.7.2 **Market Disposal:** Either to another developer or a supplier who would use these pods or breakdown into components for other similar construction methods and or council sites.
- 3.7.3 **Demolition / Steel disposal:** This would be the least preferred option of disposal and would likely receive a lower return, however, would remove future and ongoing expenses relating to security, storage and maintenance.
- 3.7.4 **Future use:**
- 3.7.5 It should be noted that beyond the decision to pursue all cost recovery avenues, Officers are exploring other uses for the sites.
- 3.7.6 The priority being to maximise delivery, testing traditional build options and seeking valuations on the sites with planning consent having been granted.
- 3.7.7 Officers will work to identify solutions that enable the delivery of a revised housing scheme which includes affordable housing on one or both sites. We will examine several

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delivery and partnering options for these sites. If the decision is taken to dispose, Officers will bring back options for future delivery within a separate report Autumn 2023.

4. Financial implications

4.1 As identified within Part 2 report

5. Legal implications

5.1 This report seeks approval to remove the Home Park and Edward Street development projects from the Building for Lewisham Programme. The Council has sufficient powers to do this. The Council must comply with grant funding conditions applicable to the sites, particularly in relation to repayment of funding because of the removal of these schemes.

5.2 The Council must at all times be mindful of its fiduciary duties in acting as a trustee of Council tax and public sector income on behalf of its rate and taxpayers, including the obligation to act efficiently in a "business-like manner" after proper consideration of the risks and rewards of the proposed course of action. The decisions taken because of the recommendations in this report must be taken in the context of this fiduciary duty.

5.3 The contract for the delivery of the schemes was between Lewisham Homes Limited and the contractor and Lewisham Homes are progressing with claims to seek to recover losses because of the insolvency of the contractor and have received advice from their own lawyers in this regard. Lewisham Homes are the legal owners of the completed modular housing units and storage fees will be payable by Lewisham Homes. Options for the ongoing storage and disposal of the units is a decision that must be taken by Lewisham Homes.

5.4 Any decision about the future development of these sites will be a matter for Mayor and Cabinet in a separate report.

5.5 Any future procurement of works in respect of the sites must comply with the Public Contracts Regulations 2015 (or, if applicable, its replacement legislation) and the Council's constitution.

6. Equalities implications

6.1 Despite the loss of Housing Units previously approved, we will work to identify solutions that enable the delivery of a revised housing scheme which includes affordable housing on one or both sites.

7. Climate change and environmental implications

7.1 Existing planning consents obtained for both sites were in line with the standards expected by the Council and the GLA.

7.2 Due to the nature of this report and recommendations set out it is likely the future development proposals for these sites will change and therefore climate change and environmental implications will be reviewed once revised development options are prepared

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for approval. These will be set out within any subsequent approval to Mayor and Cabinet.

7.3 Whilst options are considered for both sites, every effort will be made to enhance the natural environment, enhance landscape and amenity space with any future development options considered.

8. Crime and disorder implications

8.1 The sites are currently managed and secure with adequate hoarding and regular site inspections taking place.

9. Health and wellbeing implications

9.1 There are no direct health and wellbeing implications arising from this report

10. Social Value Implications

10.1 The council is an officially accredited London Living Wage (LLW) Employer and is committed to ensuring that, where appropriate, contractors and subcontractors engaged by the council to provide works or services within Lewisham pay their staff at a minimum rate equivalent to the LLW rate.

10.2 Any future development options for these sites will be expected to meet LLW requirements and any associated contract conditions requiring the payment of LLW will be included in the service specification and contract documents.

11. Report author(s) and contact

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12. Appendices

None

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