

Agenda Item 20

Name of decision-maker Council	DATE 20 th November 2024
REPORT/DECISION TITLE Affordable Housing Programme – First 93 units across 4 sites	WARD(S) Cricket Green Ward St Helier Ward Figges Marsh Ward
CHIEF OFFICER James McGinlay, Interim Executive Director Housing and Sustainable Development	CABINET/LEAD MEMBER Councillor Andrew Judge – Cabinet Member for Housing and Sustainable Development
DECISION CLASSIFICATION Non-exempt report <i>Exempt Appendix A/Fully Exempt</i> <i>Exempt by virtue of paragraph 3 of Schedule 12A to the Local Government Act 1972 (as amended): Information relating to the financial or business affairs of any particular person including the authority holding that information.</i>	IS THE FINAL DECISION ON THE RECOMMENDATIONS IN THIS REPORT TO BE MADE AT THIS MEETING? Yes

1. Recommendations:

That Council:

- A. Note the progress on the programme for the delivery of 93 new affordable homes.
- B. Note the contents of Section 4 of the report with the financial detail set out in Exempt Appendix A summarising the financial impact of the revised scheme and approve the increase to the capital programme and its funding totaling £27.87m.

2 Purpose of Report and Executive Summary

- 2.1 The Council is progressing with the delivery of 93 new affordable social rent homes on 4 sites as part of its ambition to enable the delivery of 400 new affordable homes. This is the first phase of the programme that will deliver well designed, energy efficient and genuinely affordable homes for the residents of Merton. The Council has invested in this programme, supported by the Mayor of London. The Council agreed to deliver

these through a collaboration agreement with London and Quadrant Housing Trust (L&Q) who will provide construction management services for the council.

- 2.2 It is some time since the original schemes on these 4 sites were designed and over recent months the Council has progressed the detailed design of the homes, securing amended planning consents to incorporate Passive House environmental and sustainability principles and other design amendments. As the designs have progressed, further work has been undertaken to understand the costs of the schemes and to test these through a soft-market testing exercise with contractors. L&Q have compiled a bill of quantities to provide more certainty about the costs. The results of this exercise show there is a significant increase in costs since the original budget was set. This increase is due to several factors including inflation and increases in construction costs; the inclusion of amended specifications for environmental measures to meet new Building Regulations and to deliver Passive House principles and a more detailed understanding of the construction logistics required on the sites.
- 2.3 The Council created a budget in March 2023 for the delivery of affordable homes. However, due to the increased costs the Council needs to increase this budget, and approval is sought through this report to add additional funds to the capital programme. The details of the amount required is set out in Exempt Appendix A.
- 2.4 The Council has secured grant funding from the GLA under the Homes for Londoners: Affordable Homes Programme 2021 – 2026 and this will contribute to funding the overall programme. The aim of the programme is to increase the supply of affordable housing in London, which is consistent with the Council's aim to provide homes at a decent standard and genuinely affordable level. It is the Council's intention that these units will be let at Social Rent levels and will help meet the demand for affordable homes in the area.
- 2.5 L&Q are preparing the invitations to tender for the construction packages which will be issued with responses expected from early in the new year onwards. The final costs for the schemes will not be known until those tenders are returned. Provided the tendered sums are within the budget scope agreed by Council, the Authority will enter into contracts with the selected contractors. Approval was previously given by Cabinet on 14th October 2024 for the Executive Director for Housing and Sustainable Development and the Executive Director of Finance and Digital in consultation with the Cabinet Member for Housing and Sustainability and the Cabinet Member for Finance and Corporate Services to enter into those contracts.

3. Links to the Merton Priorities

- 3.1 This report relates to the Council's Strategic priority **Building a Sustainable Future** and the objective to **Build 400 homes on council owned land and ensure the increased supply of affordable homes in the borough**. Implementing the recommendations in this report will progress the delivery of 93 new affordable homes on council owned land. 100% of these homes will be in the Social Rent category and delivery of these homes using Passive House principles will support the Council's **Zero Carbon by 2030 Policy** and the delivery of high-quality social rent housing for

residents of the Borough is supportive of the **Civic Pride priority** in the Councils' programme.

4. Introduction and Background

- 4.1 To implement the Council's ambition to deliver 400 new affordable homes in the borough on council-owned land the Council identified 4 sites in its ownership and agreed in October 2022 that the sites would be used to deliver affordable housing. These sites already had proposals worked up to deliver 93 homes that had been considered by the Development and Planning Applications Committee. The four sites are:
- Elm Nursery Car Park, Mitcham CR4 3TA (21 units);
 - Raleigh Gardens Car Park Mitcham CR4 2JB (36 units);
 - Land at Canons, Madeira Road, Mitcham CR4 4HD (18 Units); and
 - Farm Road Church, Farm Road, Morden SM4 6RA (18 units).
- 4.2 In anticipation of the Council delivering these first 93 homes a capital budget of £29m was created and added to the Capital Programme starting in 2023/24 for 4 years. This was based on a high-level estimate of the delivery of the homes at that time.
- 4.3 In June 2023, Cabinet provided approval for the Council to enter into a Collaboration Agreement with London & Quadrant Housing Trust (L&Q) to deliver the 93 homes for the Council. Following consideration by the Council of a range of delivery options, including direct delivery by the council, it was concluded that working with L&Q was the most cost-effective and quickest solution to deliver the housing.
- 4.4 Working with L&Q and the architects Weston Williamson and the Professional Design Team, the designs for the housing schemes have been updated and refined to incorporate new building regulations, Passive House principles, reviewed for compliance with the London Plan and GLA Grant requirements. Given the evident increase in development costs (something that we have seen reported by many other London Councils) officers have also worked with L&Q to incorporate cost savings where possible. Planning consent was granted for these changes in August 2024.
- 4.5 Quantity Surveyors at L&Q have revisited the costs of delivering the homes and engaged with construction contractors to soft market test the prices of key construction packages. A bill of quantities has been prepared in July 2024 providing more up to date and accurate costs. This has resulted in higher estimated costs than previously anticipated in 2023. The key drivers of the cost increases are:
- Inflation particularly of the construction costs due to significant increases in building materials and construction labour and a generally risk-averse developer market.
 - Additional work and measures required to implement Passive House principles and improve environmental performance.
 - Detailed mapping of the logistics plans identifying additional third-party rights required and more complicated logistics.

- Additional costs for the Council to fund including legal fees, monitoring of the construction and independent advisors.
- Consideration of the amount of contingency to be included.

These factors have increased the estimated budget required. The proposed new budget required is set out in the confidential appendix and includes contingency and the Council's direct costs.

- 4.6 In order to continue with the procurement and enter into contracts when tenders are received additional budget will need to be allocated to the Council Capital programme. Up to £27.87m will be required - some of this increase is secured from additional GLA grant from the Mayor of London's Affordable Homes Programme 2021-2026 for which the council now needs to enter into a grant agreement. The remainder will need to be found by Merton through internal borrowing. We will continue to investigate the possibility of further external funding. In particular, the Council will continue to work with the GLA to look at the funding ratio for construction of these homes and consider if any additional grant can be secured.

Finance and Other Resources

4.7 Capital Programme

- 4.7.1 As the Council will be an accountable body in respect of the grant funding and in accordance with relevant Financial Regulations the Executive Director of Finance & Digital has delegated power for treasury management including borrowing and can decide upon methods of capital financing. It is confirmed in the Financial Implications that the Executive Director of Finance & Digital approves entry into the grant agreement.
- 4.7.2 The approved capital programme contains the following provision/budget and funding for this scheme of £29.13m.
- 4.7.3 Based on the compilation of a Bill of Quantities costs forecast by L&Q, reviewing development costs of other housing delivery programmes and adding Merton's estimated capital costs it is estimated that the budget in the approved programme should be increased significantly as shown in Exempt Appendix A.
- 4.7.4 It should be noted that there are risks to the estimates of costs set out, and that until tenders are received and other areas of costs/estimates are finalised, these cost forecasts will continue to be subject to change.

4.8 Revenue

- 4.8.1 There are a number of potential impacts on the Council's revenue budgets from these schemes:
- 4.8.2 Staffing resources. To oversee the development and work longer term on the management of these and other units to be developed the Council has employed a small number of staff and consultants and developed an outline of a longer-term staffing structure. There will be a continuing requirement to recruit resources.

However, we will endeavour to capitalise as much of these staff costs as possible. To ensure that we can meet staffing costs required, the costs associated with the sites and costs associated with the wider development proposals it is recommended that an earmarked reserve will be established to fund those costs and those staffing costs which cannot be capitalised pending a more permanent solution to funding the housing delivery team.

To that end, an earmarked reserve of £1 million to fund these costs will be created, as well as acting as a cushion against unforeseen costs, mitigation of risk and a source to fund non-capitalisable costs to ensure successful delivery of this key project. This is a major investment for the Council carrying significant financial risks as set out in the report and hence it is considered important that there is sufficient flexibility in the budget to employ the staff resources required

4.8.3 Once the schemes are complete the authority will need to establish revenue budgets for the management and maintenance of the properties.

4.8.4 It should be noted that these costings reflect our best estimate based on the information available at the time of drafting the report.

4.9 **Calculation of Prudential and Key Indicators**

4.9.1 Borrowing costs. The most significant revenue impact on the Council will be in funding the borrowing costs associated with these schemes. The proposals contained in this report will result in a significant increase in internal borrowing to that considered when setting the budget as part of the budget process as set out in Exempt Appendix A. Finance officers have recalculated the key corporate and treasury (prudential) indicators that this decision will have.

4.9.2 The Minimum Revenue Provision will increase by £1.35m. However, as referred to in the viability section below this will to some extent (though not fully) be offset by rental income from the new properties.

4.9.3 As at 2030-31 the Capital Financing Requirement (CFR) would be just under £19.6m higher than that required by the current programme, current projections (allowing for slippage) would mean that the need to externally borrow will move forward by approximately one financial year should the Capital Programme stay as it is.

4.10 **Viability Modelling**

4.10.1 The Council has undertaken viability modelling with the GLA to achieve the current grant and is continuing to develop modelling as costs and other factors change.

4.10.2 To enable the financial modelling of the site a number of key appraisal assumptions must be made. These include the build programme, an estimate of the total cost of developing the scheme, net of any capital income (e.g. GLA grant funding), and those assumptions relating to the long-term management and operation of the scheme (i.e. the rental income net of the operating costs LBM will incur as part of fulfilling its landlord responsibilities).

4.10.3 All 93 of the units developed will be affordable housing and are on small, non-contiguous sites, and hence, in the current market, the Authority would expect any modelling to show a deficit in purely financial terms.

- 4.10.4 However, in assessing viability and “worth” it must be remembered that these schemes will provide 93 units of much needed social housing. To break even in simple development financial terms the Authority would need to reduce costs through a combination of reducing the specification, reducing the number of sites being developed or considering mixed tenure including higher rental values or private sale. This would not be in line with the Council’s stated priorities but importantly there also other factors to consider.
- 4.11 Homelessness/Temporary Accommodation – like all other Councils in London the Council has seen significant increase in homelessness and hence demand in its temporary accommodation budget. The provision of new build housing will increase the overall supply, helping to reduce the need for temporary accommodation.
- 4.12 Wider health and well-being benefits – there are numerous reports by the Kings Fund, Joseph Rowntree Foundation and many others into the damaging impact of insecure housing on families and individuals. It is incredibly difficult to assign an accurate financial value to such impact (though there are reports that do this at a national level) but there is a clear social well-being benefit that can be translated into benefits for the wider public sector from the provision of social housing. [003]
- 4.13 Tax Implications
- 4.13.1 To optimise Merton’s tax position and minimise its impact Merton is seeking specialist legal/tax advice.

5. Available Options

- 5.1 The Council has already considered different options to deliver the 93 social rent homes and concluded, as set out in the June 2023 Cabinet report, that delivering the homes through a collaboration agreement with L&Q is the most cost-effective solution. L&Q are not charging any profit for their services. Given the drivers for the increased costs, reconsidering other methods of delivery is unlikely to result in cost savings.
- 5.1.1 In light of the cost increases, the Council could consider other options such as the following:
- Option 1 - To not proceed with the development of the 93 homes** resulting in no affordable council homes delivered by 2026 with significant abortive costs incurred in design of the homes
- Option 2 - To reduce the specification of the homes for example, to not include the additional measures to deliver Passive House principles** – this is unlikely to achieve significant savings due to a further redesign being required and revised planning consent that will delay the timetable for delivery. It will also not achieve the council’s ambitions on net zero.
- Option 3 - To not proceed with one or more of the sites** – reducing the number of homes delivered.
- Option 4 - To seek additional external grant funding** – all additional grant funding opportunities will be explored but very unlikely to cover all additional costs. The GLA is the most likely source for additional grant, although the GLA has already agreed to

provide significant grant funding and are limited to funding 50% of the overall development costs.

5.2 Preferred Option

5.2.1 The preferred option is to continue with the development of the 4 sites and make additional budget available. Officers will discuss with the GLA any potential for additional funding and continue to monitor any other sources including S106 affordable housing contributions and anything else Government may make available to accelerate affordable housing delivery.

6. Reasons for Recommendations

6.1 To enable the schemes to progress and homes to be delivered

7. Consultation

7.1 Statutory consultation for the planning applications was undertaken ensuring residents are aware of the proposals for the 4 sites. The Council will prepare an engagement plan to inform and work with residents and businesses in the vicinity of the four sites affected in the lead up to construction commencement dates.

8. Next Steps & Timetable: Communication and Implementation of the Decision

8.1 The Invitations to Tender will be issued to the market with return dates expected from early in 2025. Following receipt of the tenders the Council and L&Q will select the most economically advantageous and enter into contract.

8.2 Contractors will commence site set up and preparation with a start on site scheduled from March 2025.

8.3 A consultation and engagement plan is being prepared to ensure timely communications with residents, businesses and other stakeholders that may be affected by the construction works on the sites.

9. Report Appendices

9.1 The following documents are to be published with and form part of the report:

Exempt Appendix A: Revised Capital Budget for New Homes

10. Background Papers

None

11. Cross-Cutting Issues and Implications and Sign-Off

Issue	Implications	Sign-off
Legal including Human Rights Act	Full Council is responsible for approving the policy framework and budget within which the Council operates. It is also responsible for approving and monitoring compliance	<i>Jennifer Muller - Principal Lawyer – Property and Planning</i>

Issue	Implications	Sign-off
	<p>with the authority's overall framework of accountability and control.</p> <p>Full Council is also responsible for agreeing variations to approved budgets, plans and strategies forming the policy framework and for determining the circumstances in which a decision will be deemed to be contrary to the budget or policy framework.</p> <p>The Council should ensure that any contracts entered into in connection with the delivery of the development schemes include the same terms and conditions as those contained in the GLA Grant Funding Agreement to fulfil its obligations thereunder.</p>	28/10/2024
Finance and other resources	Financial Implications outlined in the report	<i>Asad Mushtaq</i>

<p>Equalities</p>	<p>Decision-makers are reminded of the requirement under the Public Sector Equality Duty (s149 of the Equality Act 2010) to have due regard to (i) eliminate unlawful discrimination, harassment, victimisation and other conduct prohibited by the Act, (ii) advance equality of opportunity between people from different groups, and (iii) foster good relations between people from different groups.</p> <p>An EQIA has been undertaken and the following key impacts identified:</p> <ul style="list-style-type: none"> - <u>Positive impact on people with disabilities</u> - 9 new homes designed to wheelchair standards therefore increasing the number of affordable homes in the borough for wheelchair users. 4 <u>Negative impacts during construction (temporary) on older people, people with disabilities and those with caring responsibilities</u> who live in neighbouring properties that could be subject to noise and disruption. These people during periods of noisy construction activity. – <i>mitigation – good advance communication with neighbours about the works</i> 	<p><i>Lucy Taylor – Regeneration and Housing Consultant.</i></p>
<p>Climate change</p>	<ul style="list-style-type: none"> - The 93 homes will be built to Passive House principles and standards. - Contractors will be required to demonstrate they are taking measures to reduce adverse environmental impacts through construction management plans and waste and recycling management plans - Landscaping plans will be designed to incorporate Sustainable Urban Drainage (SUDS) and increase biodiversity where possible. 	<p><i>Lucy Taylor – Regeneration and Housing Consultant.</i></p>
<p>Procurement & Social Value</p>	<p>The procurement of the construction of the 93 homes through L&Q has been considered at the Council’s Procurement Board. The</p>	<p><i>Lucy Taylor – Regeneration</i></p>

	invitations to tender issued by L&Q on behalf of the Council will set out requirements for contractors to confirm that the London Living Wage will be paid and will include requirements to set out the added social value the contractors can provide to the borough of Merton.	<i>and Housing Consultant.</i>
Risk management	A Risk Register has been produced for this programme. Key risks identified for the project are: <ul style="list-style-type: none"> - Increased construction costs due to inflation - Construction logistics to deliver the schemes due to small sites and limited availability of space for materials and site management. 	<i>Lucy Taylor – Regeneration and Housing Consultant.</i>
Health and Safety	The appointed construction contractors will be responsible for managing the sites whilst the construction is taking place and for complying with all health and safety legislation. There are no specific Health and Safety implications for the Council.	<i>Lucy Taylor – Regeneration and Housing Consultant.</i>
Health and wellbeing	The proposal will provide 93 new homes designed to Passive House principles providing high quality housing with a healthy living environment.	<i>Lucy Taylor – Regeneration and Housing Consultant.</i>
Executive Director	<i>Clearance/Approval of Report</i>	<i>James McGinlay, Interim Executive Director of Housing and Sustainability</i>
Cabinet Member/s	<i>Clearance/Approval of Report</i>	<i>Councillor Judge Cabinet Member for Housing and Sustainability 12/11/24</i>
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