

## Report of Chief Officer, Housing Leeds

### Report to Director of Communities, Housing and Environment

**Date: September 2022**

**Subject: Inflationary uplift to the responsive repairs, voids & cyclical maintenance delivery contract (Mears) in the West of Leeds**

Are specific electoral wards affected?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
If yes, name(s) of ward(s): Adel & Wharfedale, Armley, Bramley & Stanningley, Calverley & Farsley, City & Hunslet, Farnley & Wortley, Guiseley & Rawdon, Headingley & Hyde Park, Horsforth, Kirkstall, Otley & Yeadon, Pudsey, Weetwood	
Are there implications for equality and diversity and cohesion and integration?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
Is the decision eligible for call-in?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
Does the report contain confidential or exempt information?	<input checked="" type="checkbox"/> Yes <input type="checkbox"/> No
If relevant, access to information procedure rule number: <i>Rule 10.4 (3). The appendix contains commercially sensitive information, which if disclosed, would adversely affect the business of the Council and external parties and as such, the public interest in maintaining the exemption in relation to the confidential Appendix outweighs the public interest in disclosing the information / financial details at this time.</i> Appendix number: Appendix A	

### Summary of main issues

1. The council owns and manages approx. 19,000 homes in the West area of the city. The contract for the delivery of Responsive Repairs, Voids and Cyclical Maintenance (RR, V & CM) work in this area was awarded to Mears Group in April 2021 and commenced on 1<sup>st</sup> October 2021. The contract value is c.£14.5m p/a and is for a fixed 5 year term with no option to extend beyond this period.
2. The terms of the contract between Housing Leeds and Mears does not contain any price reviews during the 5 year period, i.e. the tendered Schedule of Rates for work delivered is fixed for the entirety of the contract.

3. However, since the commencement of the contract, the industry, as with many areas of the economy, has seen significant challenge associated with shortages and increased costs of materials, labour and overheads (e.g. building costs, fuel and energy prices).
4. As such, in June 2022 Mears issued an Early Warning Notice (EWN) to Leeds City Council, noting “...*extraordinary increase in inflation in the period since the works were tendered in 2020,*” essentially meaning that the prices tendered were unable to be sustained for the remainder of the contract period. A copy of this EWN is included as a confidential appendix.
5. Upon receipt of the EWN, Housing Leeds engaged colleagues in Procurement and Commercial Service (PACS) and Finance, in line with the corporate guidance issued by PACS, to ensure internal governance processes and Council guidance were followed in assessing how most appropriately to respond to the situation.
6. An Options Appraisal was undertaken to ensure all available options were assessed, ensuring that Housing Leeds continued to deliver these essential, statutory services while ensuring a preferred option also delivered best value to the council.
7. As the pressures highlighted by Mears were objectively demonstrable, it was agreed that the most appropriate response was for the Council to negotiate with Mears to agree an uplift in the current Schedule of Rates.
8. These negotiations were informally concluded in September 2022, subject to appropriate governance and approvals.

## **Recommendations**

That the Director of Communities, Housing and Environment notes the content of the report, and:

1. Approves a one-off increase of 9.25% in the Schedule of Rates for the Responsive Repairs, Voids and Cyclical Maintenance contract between Leeds City Council and Mears Group.
2. Approves the application of this increase in rates from 1<sup>st</sup> October 2022.

## **1. Purpose of this report**

- 1.1.** To seek the Director of Communities, Housing and Environment approval to increase the value of the Schedule of Rates for the delivery of Responsive Repairs, Voids and Cyclical Maintenance by 9.25%, applicable from 1<sup>st</sup> October 2022.
- 1.2.** The report also provides background and information in relation to these recommendations.

## **2. Background information**

- 2.1.** The council owns and manages approx. 19,000 homes in the West area of the city. The contract for the delivery of Responsive Repairs, Voids and Cyclical Maintenance (RR, V & CM) work in this area was awarded to Mears Group in April 2021 following a competitive tender exercise and commenced on 1st October 2021. The contract value is c.£14.5m p/a and is for a fixed 5 year term with no option to extend beyond this period.
- 2.2.** The remaining areas of the city, East and South, are delivered by the council's internal service provider, LBS, the latter of these areas being in-sourced from an external contractor in July 2021.
- 2.3.** The terms of the contract between Housing Leeds and Mears does not contain any price reviews during the 5 year period, i.e. the tendered Schedule of Rates for work delivered is fixed for the entirety of the contract. This is contrary to a number of other comparable contracts held by the council, where price reviews are linked to particular price indices.
- 2.4.** The rationale for the exclusion of such a price review mechanism in the RR, V & CM contract was that, at the point of development of the contract documents and terms in 2019 and 2020, the 'market place' for such services had seen over a decade of stability in terms of inflation with extremely low interest rates and stable growth with Bank of England interest rates consistently below 1% since 2009. At the point at which tenders were submitted (December 2020), this rate stood at 0.75%. The Annual inflation rate of the Consumer Price Index in the United Kingdom averaged 2.64% for the period 2009 to 2020.
- 2.5.** As such, in-order to achieve some degree of cost certainty for the Council, it was felt that interested parties bidding for the contract could comfortably predict the rate of interest over the full contract period and build this into their tender submissions. Effectively transferring risk from the council to the contractor however assuming minimal risk to the council/council tenants in terms of risk to the delivery of statutory repairs and maintenance functions.
- 2.6.** However, since prices were submitted and particularly since the start of the contract in October 2021, the maintenance industry, as with many areas of the economy, has seen significant challenge associated with increased costs of

materials, labour and overheads, particularly utilities costs, fuel and energy prices.

- 2.7. This has contributed to The Consumer Price Index increasing to 4.1% in 2021 (from 1.5% in 2020) and it is predicted to close at around 11.8% in 2022.
- 2.8. In April 2022, the Office of Budget Responsibility wrote *“Inflation in 2022 is at its highest rate in around 40 years. The increase is driven primarily by higher gas prices feeding into sharp rises in domestic energy bills, alongside higher fuel prices and global goods inflation...”* It also noted that these pressures were unlikely to return to target until the end of 2025.
- 2.9. As a result, in June 2022 Mears issued an Early Warning Notice (EWN) to Leeds City Council, noting *“...extraordinary increase in inflation in the period since the works were tendered in 2020,”* essentially meaning that the prices tendered were unable to be sustained for the remainder of the contract period, putting the future viability of the contract in jeopardy and causing a significant risk to the continued delivery of statutory services to tenants living in the West areas of the city.
- 2.10. Upon receipt of the EWN, Housing Leeds engaged colleagues in PACS and Finance to ensure internal governance processes and Council guidance were followed in assessing how most appropriately to respond to the situation.
- 2.11. An Options Appraisal was undertaken to ensure all available options were assessed, ensuring that Housing Leeds continued to deliver these essential, statutory services while ensuring a preferred option also delivered best value to the council.
- 2.12. As the pressures highlighted by Mears were objectively demonstrable, it was agreed that the most appropriate response was for the Council to negotiate with Mears to agree an uplift in the current Schedule of Rates.
- 2.13. These negotiations were informally concluded in September 2022, subject to appropriate governance and approvals. The outcome of these negotiations is the recommendation that a 9.25% uplift to the Schedule of Rates is applied from 1<sup>st</sup> October 2022.
- 2.14. This recommended uplift does **not** represent the introduction of an annual review of contract prices which would be a variation to the original agreement), but instead a **one-off** increase to the tendered rates to be applied for the remaining 4 years of the contract.

### 3. Main issues

- 3.1. Responsive repairs, voids and cyclical maintenance to council-owned homes is an essential service for the residents of Housing Leeds, ensuring homes are well maintained in a safe manner, compliant with a range of health and safety legislation and meet the needs of Housing Leeds’ diverse customer base.

- 3.2. Failure to deliver an effective service would not only have significant reputational damage for Leeds City Council, but also risk the council's ability to deliver a range of statutory services, including fire safety works and electrical safety inspections as well as the reservicing of empty homes.
- 3.3. Due to the unprecedented situation being seen in the industry, including major disruption to material supplies and labour shortages, as well as increases in energy and fuel costs, the cost of delivering these services has increased significantly since the commencement of the contract. This can be evidenced utilising financial tracking indices such as the *Consumer Prices Index*, as well as more industry specific measures such as *BCIS Local Authority Maintenance Cost Index – Services* and *BCIS General Building Cost Index*, all of which have seen steep increases over the course of the last 18-24 months.
- 3.4. As a result, the tendered rates submitted by Mears for delivery of services in the West of the city meant the contract was no longer financially viable. This resulted in the submission of an Early Warning Notice to Leeds City Council requesting an increase in the tendered rates.
- 3.5. Following receipt of the EWN an Options Appraisal was undertaken to ensure all available options were assessed, ensuring that Housing Leeds continued to deliver these essential, statutory services while ensuring a preferred option also delivered best value to the council. The options considered were:
  - 3.5.1. **Refuse the request and remain on tendered rates.** This option was ruled out on the basis that it would likely lead to termination of the contract on the basis of financial viability.
  - 3.5.2. **Reprocure the contract.** This option was ruled out on the basis that re-tendered rates would be significantly higher than those previously submitted as a result of the market pressures highlighted above, plus the ongoing instability in the market.
  - 3.5.3. **Insource service to LBS.** This option was ruled out on the basis that LBS has recently undergone significant expansion in the South of the city and remains in the 'normalisation' phase of delivery. Further expansion at this time was deemed too high a risk, putting the effectiveness of the service across the city at risk.
  - 3.5.4. **Negotiate with Mears to reach a mutually agreeable position.** This was identified as the preferred option on the basis of 'best value' (i.e. would still represent the least costly option for Housing Leeds) and operational continuity.
- 3.6. Colleagues in Finance and PACS were engaged throughout this process to ensure all options and negotiations followed LCC guidance and governance processes.
- 3.7. The outcome of the subsequent negotiations with Mears have resulted in the recommendation of a one-off 9.25% increase to the Schedule of Rates,

applicable from 1<sup>st</sup> October 2022. This equates to an increase in value of approx. £680k for the remainder of FY2022/23 and £1.36m per full year thereafter.

- 3.8.** Adequate budget has been identified in the Housing Revenue Account (HRA) in FY2022/23 to manage this pressure and built into future budget provision for future years.

## **4. Corporate considerations**

### **4.1. Consultation and engagement**

- 4.1.1. The Director of Communities, Housing and Environment has been consulted on the proposed recommendations of this report.
- 4.1.2. The Executive Member for Communities, Housing and Environment has been consulted on the proposed recommendations of this report.
- 4.1.3. Senior colleagues in Finance, including Head of Finance, have been consulted and actively involved in the negotiations.
- 4.1.4. Senior colleagues in Procurement and Commercial Services (PACS) have been consulted and actively involved in the Options Appraisal process.

### **4.2. Equality and diversity / cohesion and integration**

- 4.2.1. An Equality, Diversity, Cohesion and Integration screening and impact assessment has been completed and an appropriate action plan has been put in place. The assessment is attached.

### **4.3. Council policies and the Best Council Objectives**

- 4.3.1. Corporate guidance and policies have been followed throughout this process, including those specifically released by PACS in relation to contractor applications for increased costs.
- 4.3.2. The recommendation supports the Best Council Objectives by offering best value for money and operational continuity.

### **4.4. Resources and value for money**

- 4.4.1. The outcome of the negotiations with Mears have resulted in the recommendation of a one-off 9.25% increase to the Schedule of Rates, applicable from 1st October 2022. This equates to an increase in value of approx. £680k for the remainder of FY2022/23 and £1.36m per full year thereafter.

4.4.2. Adequate budget has been identified in the Housing Revenue Account (HRA) in FY2022/23 to manage this pressure and built into future budget provision for future years.

4.4.3. As part of the consideration of the other options considered (see 3.5) it was identified that significant financial and staffing resources would need to be employed to deliver any of the options considered non-preferred. The staffing and internal resources in particular are currently stretched to maximum capacity and delivering a procurement / in-sourcing exercise on this scale at the current time was considered to be 'very high' risk.

#### **4.5. Legal implications, access to information, and call-in**

4.5.1. The decision recommended in this report is a key decision and subject to call-in given the financial value of the recommendation for the remaining term of the contract.

4.5.2. There is a risk that other providers who tendered for the contract could challenge the decision on the basis that they tendered for the contract on the basis of a 'fixed price' Schedule of Rates for the full term. This is considered low risk due to the instability witnessed across the sector over the last 18-24 months, meaning other providers would likely be unable to stand by their tendered rates.

#### **4.6. Risk management**

4.6.1. The risks associated with this decision are recorded and managed through the Housing Leeds Property Management risk register and Housing SMT risk register.

4.6.2. In addition, the formal Risk Reduction process initiated by the submission of the Early Warning Notice in June 2022 has been followed and recorded accordingly.

### **5. Conclusions**

5.1. Given the market instability seen across the building, maintenance and construction sectors, the costs to deliver the services covered by the RR, V & CM contract have increased significantly.

5.2. This can be demonstrated by objective industry and financial mentoring indices as well as prices submitted to the council for comparable services since the commencement of this contract.

5.3. As such, the current terms of the LCC and Mears contract for delivery of these services is no longer viable to the contractor.

- 5.4.** This has resulted in the need to negotiate a one-off price increase for the future sustainability of the contract, following an appraisal of all options available to the council.

## **6. Recommendations**

- 6.1.** That the Director of Communities, Housing and Environment notes the content of the report, and:

1. Approves a one-off increase of 9.25% in the Schedule of Rates for the Responsive Repairs, Voids and Cyclical Maintenance contract between Leeds City Council and Mears Group.
2. Approves the application of this increase in rates from 1st October 2022.

## **7. Background documents**

- a. Equality, diversity, cohesion and integration impact assessment.
- b. Appendix A - Copy of Mears Early Warning Notice (Confidential).