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31 January 2018

To: All Members of the Full Council

Dear Member,

Full Council - Wednesday, 7th February, 2018

I attach a copy of the following reports for the above-mentioned meeting which were not available at the time of collation of the agenda:

5. TO CONSIDER A RESPONSE FROM THE COUNCIL IN RELATION TO THE ISSUES RAISED IN THE MOTION (PAGES 1 - 6)

Yours sincerely

Michael Kay, Democratic Services and Scrutiny Manager

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Report for: Extraordinary Full Council, 7 February 2018

Title: Haringey Development Vehicle: implications of Carillion collapse

Report authorised by : Helen Fisher, Interim Strategic Director of Regeneration, Planning and Development

Lead Officer: Dan Hawthorn, Director of Housing and Growth

Ward(s) affected: N/A

**Report for Key/
Non Key Decision:** Not for decision

1. Describe the issue under consideration

- 1.1 The Extraordinary Full Council meeting of 7 February 2018 has been called to discuss matters relating to the proposed Haringey Development Vehicle (HDV), and in particular the implications for the HDV proposals of the collapse of Carillion plc. This report provides background information to support Full Council's consideration.

2. Cabinet Member Introduction

N/A

3. Recommendations

- 3.1 That Full Council take note of the issues set out in this report, in considering matters relating to the Haringey Development Vehicle and the collapse of Carillion plc.

4. Reasons for decision

N/A

5. Alternative options considered

N/A

6. Background information

Process and decisions to date

- 6.1 Cabinet agreed at its meeting on 3 July 2017 to the selection of Lendlease Europe Holdings Limited as the successful bidder to be the Council's partner in the Haringey Development Vehicle (HDV), and to the subsequent establishment of the HDV with Lendlease or a subsidiary vehicle of Lendlease. This decision was subsequently reconfirmed at Cabinet on 20 July 2017 following a call-in of the original decision.

- 6.2 This decision followed a comprehensive OJEU procurement process, which in turn followed a November 2015 decision by Cabinet to commence procurement. That November 2015 decision was based on Cabinet's consideration of a range of options for achieving the Council's growth ambitions on Council land, and approval of the joint venture option as that most likely to achieve its objectives.
- 6.3 As part of its July 2017 decision, Cabinet gave delegated authority to officers to approve the final legal documentation necessary to establish the HDV.
- 6.4 A link to the details of the July 2017 decision – which also includes a detailed account of the preceding process – is given in section 10 below.
- 6.5 Following this Cabinet decision, a claim for judicial review of the decision was made. The case was heard in the High Court on 25 and 26 October 2017; a judgement on the case has not yet been received. The finalisation and execution of the documentation necessary to establish the HDV, and therefore the full implementation of the July 2017 Cabinet decision, has not yet taken place.

The collapse of Carillion, and implications for the HDV

- 6.6 The high-profile collapse and liquidation of Carillion plc has given rise to some concerns and questions about the HDV proposals, in light of Carillion's wide range of contracts with public sector clients, and in particular its joint venture with Sunderland Council (Siglion) which is based on a similar structure to the HDV.
- 6.7 Issues raised as a result of the Carillion collapse fall under two broad headings: first, whether the Council should remain confident in the financial strength of Lendlease, its chosen partner for the HDV; and second, what arrangements the Council has in place to minimise the likelihood and impact of any future insolvency or financial weakness on the part of Lendlease.

The financial strength of Lendlease

- 6.8 At the first stage of the OJEU procurement process for the HDV (the submission of Pre-Qualification Questionnaires), the Council stipulated a 'pass/fail' requirement for all bidders to demonstrate they had the necessary financial strength to participate in the proposed arrangement. This is in line with Government procurement guidelines. The requirement was that each bidder should have net assets of at least £100m, and an annual turnover of at least £25m for each of the preceding two years; these thresholds were set based on the anticipated scale of investment required in the HDV, which was in turn based on the preliminary financial modelling done for the Council by its commercial advisers.
- 6.9 Lendlease Europe Holdings Ltd (the specific company which has been selected as the Council's preferred bidder) comfortably met these requirements at the time the Pre-Qualification Questionnaires were submitted and assessed (Q1 of 2016). Their submission showed net assets of £314m (for the year ending 30

June 2014) and £113m (for the year ending 30 June 2013), and revenue of £1476m (2014) and £743m (2013).

- 6.10 Further, it was agreed during the procurement process that the guarantee of Lendlease Europe Holdings Ltd's financial commitments to the HDV – required by the Council as part of the procurement process – would be provided by its ultimate parent company Lendlease Corporation. As at 30 June 2017, Lendlease Corporation had revenue of approximately £9bn (A\$16.7bn) and net assets of around £3.6bn (A\$6.2bn).
- 6.11 Finally, the Council has also reviewed (in January 2018) up-to-date independent assessments of Lendlease's financial strength by Dun and Bradstreet, a leading industry data analysis firm. These assessments show that Lendlease Corporation and Lendlease Europe are 'Low Risk' and 'Minimum Risk' respectively, with both holding financial strength ratings of 5a, the highest available rating.
- 6.12 It is also worth noting the differences between the Lendlease and Carillion business models. Lendlease operates on the basis of an 'integrated business model' across the development, construction and investment sectors, with a mix of business weighted towards higher margin activities. Lendlease's business also has minimal exposure to the facilities management and outsourcing sectors, in which Carillion had substantial interests. Overall, this position illustrates how Lendlease's and Carillion's overall exposure and risk profile are substantially different, and is the basis of Lendlease's stable ratings.

Future risks to the Council

- 6.13 Notwithstanding the Council's ongoing confidence in the financial strength of Lendlease, for a contractual arrangement that is expected to last at least 15-20 years, it is prudent to put in place arrangements that anticipate and mitigate the risks to the Council either of Lendlease's liquidation, or its asset value significantly decreasing.
- 6.14 To that end, Clause 24.1.2 of the proposed Members Agreement between the Council and Lendlease (published as part of the July 2017 Cabinet papers, to which the link can be found in section 10 below) explicitly anticipates the potential both for insolvency of Lendlease, and for an unacceptable reduction in Lendlease's asset value, among other items on a list of 'Default Events' that could lead to (or risk leading to) the termination of the HDV.
- 6.15 If those Default Events are not capable of remedy, Clause 27.2.2 of the Members Agreement clearly sets out the rights of the Council in what happens next: the Council has the first option to acquire Lendlease's interest in the HDV, or to nominate a third party to acquire that interest – or to do neither, in which case the HDV is wound up. It also defines in some detail the precise procedures for protecting existing assets and live projects, and for agreeing prices, among other things. Further, before any individual development site can transfer from the Council to the HDV, the HDV must (as one of the necessary conditions) demonstrate it has the funding in place required for development to take place, which will also require Lendlease to be able to show it can meet its commitments to the HDV.

- 6.16 Therefore, while the Council has no cause for concern about Lendlease's financial position, the agreements fully anticipate the risk of situations like this happening. The agreed terms put the Council in control if such a situation arises, protecting its financial position and providing a range of options for the Council to ensure that Council property, and the HDV's own assets and projects, are not put at undue risk.
- 6.17 It is not possible to determine precisely the degree of similarity between the agreements that underpin the Siglion joint venture, and those proposed for the HDV, in terms of the specific arrangements for managing the liquidation of the private partner. In any case, while the failure of Carillion has created obvious risks to Siglion projects and to Carillion's sub-contractors, there are well-established industry processes for finding new contractors in such circumstances. It is notable that Siglion's statement on the collapse of Carillion (to which a link is provided at Section 10 below) does not anticipate that either the live development project will not be completed, or that the wider Siglion enterprise is under threat.
- 6.18 It is also worth noting that any council building new homes, even if doing so in-house, uses contractors for construction. The risks of private sector failure are therefore not unique to development partnerships with the private sector. Such development partnerships do bring a different set of risks; the decisions taken by Cabinet in respect of the HDV have described the risks to the Council, and the mitigations embedded in the relevant legal agreements and business plans. At the same time, one potential benefit of these partnerships is that a range of development risks – including contractor failure – are shared between the public authority and the private partner.

Summary

- 6.19 Given the work already done to reflect and mitigate the potential risks of Lendlease becoming insolvent or losing asset value, and more recently to update the Council's assessment of Lendlease's financial strength, it is not considered that the collapse of Carillion presents any reason to reconsider the decision to establish the HDV, or the terms on which it should be established.

7. Contribution to strategic outcomes

- 7.1 The potential contribution of the HDV to the strategic aims of the Council is set out in the July 2017 report to Cabinet.

8. Statutory Officers comments (Chief Finance Officer (including procurement), Assistant Director of Corporate Governance, Equalities)

Finance

- 8.1 It is normal practice, in evaluating potential partners at the pre-qualification stage, to assess the economic and financial standing of each bidder (or consortium where appropriate) to ensure that their financial standing and operational capabilities are of sufficient robustness to warrant inclusion at the next stage. This was confirmed in the case of Lendlease.

- 8.2 It is also normal practice, prior to contract award, for awarding authorities to confirm that nothing has changed and agencies such as Dun and Bradstreet are one of the key parties who undertake this service.
- 8.3 Once the arrangements are in place, continuous monitoring will take place to ensure that no deterioration in Lendlease's financial position occurs (e.g. regular review of accounts, profit warnings etc.). This early warning mechanism allows problems to be dealt with early. Such early warnings will permit default arrangements set out in 6.13-6.15 above to be put in place
- 8.4 However, whilst the strongest measures possible are in place to manage and mitigate risk, such risk can never be totally eliminated.
- 8.5 The processes undertaken above are appropriate and robust and as a result sufficient assurances have been received about the capacity and financial standing of Lendlease in relation to the HDV transaction.

Procurement

- 8.6 Strategic Procurement has been consulted throughout the HDV procurement process, with the Head of Procurement providing oversight and quality assurance during the process. Strategic Procurement can confirm that a robust procurement process has been followed, including assessment of all bidders' financial standing, proposed financial model and consideration in respect of mitigating risks relating to the termination of the HDV, regardless of the circumstances leading to any termination.
- 8.7 Strategic Finance recently re-ran a financial assessment on Lendlease Europe and Lendlease Corporation; both companies' financial position has strengthened since the initial evaluation during the procurement process.
- 8.8 Strategic Procurement has a process in place whereby 'key contracts' are financially monitored on a monthly basis, specifically to identify at an early stage any financial risks relating to the company emerging during the term of the contract.
- 8.9 Strategic Procurement can confirm there is no reason from a Procurement Regulation perspective that would prevent the Council continuing with the award process for Lendlease in respect of the HDV.

Legal

- 8.10 The relevant statutory framework (Local Government Act 2000) provides that where local authorities are operating under executive arrangements all functions are executive unless provided elsewhere in Regulations made under the 2000 Act or in other legislation. Full Council has power to determine matters only insofar as they are ones arising in the discharge of non-executive functions. The sense of the first resolution is to call a halt to the disposal of Council properties to the HDV. The decision of Cabinet in July 2017 includes decisions to dispose of the commercial property portfolio and the grant of an option for disposal of land at Wood Green. These were executive decisions

lawfully taken by Cabinet and Full Council does not have the power to seek to countermand or reverse these decisions. Insofar as the first resolution seeks to prevent future possible decisions on disposal it is also beyond Full Council's powers. The second and third resolutions also fall within executive powers. If Full Council nonetheless resolved in these terms, these resolutions would not bind the Executive.

Equality

The potential equality implications of the Cabinet decision to establish the Haringey Development Vehicle was set out in the papers considered and approved by Cabinet in July 2017.

9. Use of Appendices

N/A

10. Local Government (Access to Information) Act 1985

- 10.1 The decision of Cabinet to establish the Haringey Development Vehicle, and the process leading up to that decision, is set out in the papers considered and approved by Cabinet at its meeting on 20 July 2017:

<http://www.minutes.haringey.gov.uk/ielIssueDetails.aspx?IId=57530&PlanId=0&Opt=3>

- 10.2 Siglion (the joint venture between Sunderland Council and Carillion) has issued this statement on the collapse of Carillion and its implications for Siglion projects and property:

<http://siglion.co.uk/2018/01/16/siglion-statement-on-carillion-plc/>