For General Release

REPORT TO:	**CABINET 18th February 2021** **COUNCIL 29th March 2021**
SUBJECT:	**Review of Brick by Brick Croydon Ltd** **Brick by Brick Shareholder decision - the future of the company**
LEAD OFFICER:	**Katherine Kerswell – Interim Chief Executive** **Chris Buss- Consultant**
CABINET MEMBER:	**Leader of the Council** **Councillor Hamida Ali**

CORPORATE PRIORITY/POLICY CONTEXT/ AMBITIOUS FOR CROYDON

This report arises from the decisions of the meetings of Cabinet on November 25th and Full Council on November 30th regarding the initial review of Brick by Brick and other subsidiary and investment arrangements.

This further report reviews options for the future of Brick by Brick and outlines alternative arrangements to be considered for the delivery of social housing by the Council

FINANCIAL IMPACT

This report considers the options for the future of Brick by Brick and recommends a limited build out option. This option involves allowing Brick by Brick to continue building out schemes currently on site and due to complete by October 2021, market sites for disposal where completion dates are longer, and review sites no longer proposed for development. This option is to be considered in conjunction with a potential sale of the business.

The Council has a significant financial exposure with Brick by Brick through provision of over £200m in development loans including interest and therefore the options will each give the Council varying degree of risk and reward, which is further detailed within section 6 of the report. The recommended option results in Brick by Brick delaying repayment of the existing loans and potential further funding of no more than £9.99m, if required.

FORWARD PLAN KEY DECISION REFERENCE NO.: 0621CAB

The notice of the decision will specify that the decision may not be implemented until after 13.00 hours on the 6th working day following the day on which the decision was taken unless referred to the Scrutiny and Overview Committee.

1. CABINET RECOMMENDATIONS

The Leader of the Council has delegated to the Cabinet the power to make the decisions set out in the recommendations below

Cabinet is recommended to:

1.1 Consider the PwC report including recommendations at Appendix 1 of the Part B agenda and the options set out in this report; agree to proceed with the option set out as scenario 2 of that report, which is a build out of sites by Brick by Brick combined with a sale of sites under construction whilst still considering the option of a sale of the business, with a further report to Cabinet in April / May 2021.

i. Note that, with any option, there will be further costs/resourcing (in particular the sale of the business option, in order to ensure the proper advice is obtained regarding valuation, legal and financial implications) and some write off of the Council's investment (as further explained in the Part B report)

1.2 Agree that revised funding arrangements be entered into with Brick by Brick to reflect the current loan positions and proposals for the future, including, where relevant, moving to a 100% debt funding position (as opposed to 25% equity and 75% debt); extending relevant loans and repayment periods; allowing delays with repayments of existing loans; agreeing to further funding of no more than £9.99 million in relation to sites proposed for Brick by Brick to continue developing (and only where absolutely necessary within an appropriate repayment period), and:

i. Agree that the Interim Chief Executive be given delegated authority to finalise and agree the terms of new/varied funding agreements to be entered into between the Council and Brick by Brick in consultation with the Section 151 Officer and Monitoring Officer and in consultation with the Leader, Deputy Leader and Cabinet Member for Resources and Financial Governance.
ii. Note the progress of the loan agreement review (recommendation 19 of the Report in the Public Interest), as detailed in paragraphs 3.13-3.15 of this report.
iii. Note the advice at paragraph within the Part B paper regarding the legal implications of these proposed revised funding arrangements
iv. Agree, where practically possible, to apply all funds being received from Brick by Brick first to the accrued interest and any subsequent funding will be used to pay back the principle loans

1.3 Agree for the necessary steps to be taken, in accordance with the Council's Tenders and Contracts Regulations, to appoint marketing agents to consider the disposal options for the College Green site (note, this is the site adjacent to Fairfield Halls which was due to transfer to Brick by Brick, but is currently held by the Council); the outcome of this options appraisal shall be reported back to Cabinet in accordance with the Council's governance processes.

1.4 Agree for the Council to review those sites Brick by Brick propose not to develop, as identified in Appendix 4, and to receive a future report to Cabinet on the potential use and future of each site (note, these are sites that had originally been intended to be transferred to Brick by Brick but are still held by the Council).

1.5 Agree that the plans to transfer the four sites identified in Appendix 4 from the Council to Brick by Brick proceed and, note, these sites will then be dealt with in accordance with recommendation 1.9 below.

1.6 Approve that the Council's Housing Revenue Account (HRA) can acquire residential units from Brick by Brick as part of this review and note that the concurrent report to Cabinet regarding the arrangements for the future development of social housing within the Housing Revenue Account business plan will include Brick By Brick developments sites as potential development options. The acquisition and development will be subject to a review of affordability and HRA revenue implications.

The Cabinet, on behalf of the Council, exercising its functions as sole shareholder of Brick By Brick Croydon Ltd, is recommended to:

1.7 Agree that Brick by Brick continue to build out those schemes currently on site and due to complete by October 2021 (as identified in Appendix 2)

1.8 Agree that, in the event risks arise which affect timely completion of those sites referred to in Recommendation 1.7, agree that:

  i. Brick by Brick shall report to the Council's Interim Chief Executive regarding those risks, including any development, operational, legal or other risks;
  ii. The Council's Interim Chief Executive, in consultation with the Section 151 Officer and Leader, be authorised to decide:
     a. whether the risks are such that selling the site(s) urgently would be more economically advantageous and, in those circumstances, shall have the ability to authorise Brick by Brick to sell those relevant sites; or
     b. whether a further review is to be carried out and reported to Cabinet for a decision.

1.9 Agree that, for those sites which have estimated completion dates beyond October 2021 (as identified in Appendix 2), Brick by Brick be authorised to:

  i. market the sites for sale and report back to the Council's Interim Chief Executive and Section 151 Officer regarding offers received;
  ii. Subject to any objection by the Council's Interim Chief Executive in consultation with the Section 151 Officer and the Leader (note, this is to allow the Council the opportunity to consider whether continued build out of these sites might be more cost effective than offers received), sell those sites and, where necessary, novate any relevant contracts, such as building contracts, to the purchasers (for the avoidance of doubt, should the Council's Interim Chief Executive object, Brick by Brick shall not have the shareholder's authority to sell those sites).

1.10 Agree with the recommendation of the board of Brick by Brick to depart from the current Business Plan and no longer develop any site other than those sites identified in Appendix 2 (note, potential future transfers of interests in the work already undertaken will be the subject of a future report to Cabinet in accordance with recommendation 1.5 above).

1.11 Agree that these recommendations be adopted by way of shareholder resolution as revisions to the Business Plan of Brick by Brick Croydon Ltd, thereby requiring the company and Directors of the company to act on these recommendations and to carry out all necessary actions to give effect to them.

1.12 Require the Board of Brick by Brick to prepare and submit a revised Business Plan (by no later than May Cabinet) for adoption by the Council as shareholder, reflecting the decisions made under this report and to include the consequential impact on staffing and other relevant matters.

COUNCIL RECOMMENDATIONS

1.13 The Council is asked to note the recommendations set out above, which are to be considered by Cabinet on 18 February 2021 and that Council shall receive a verbal update in respect of the outcome.

2. EXECUTIVE SUMMARY

2.1 This purpose of this report is to receive and note the reported outcomes of the second stage of the strategic review with particular regard to the future activities of Brick by Brick. The review concludes that, in order to minimise the risk exposure to the Council and thus minimise the future losses to the Council, a decision on the future operation of Brick by Brick should be taken. This report outlines the options for Cabinet to consider in regard to the future of the company (and therefore changes to its Business Plan).

2.2 The options contained in this report specifically address the sites that have been transferred to Brick by Brick or are also under contract and those which have not yet commenced and considers whether they should be built out by Brick by Brick and possibly sold on with novated contacts at a later date .

2.3 The report recommends that the Council undertakes a review of those sites not yet transferred to Brick by Brick (and as such not being built out by Brick by Brick) to determine their future use, including whether some of the sites should be retained for the provision of new build social housing by the Council within the Housing Revenue account.

2.4 The impact of a decision to proceed with the recommendations in this report on Brick by Brick means that the organisation will be in a run down situation whilst sites are completed or disposed of. This will impact staffing within Brick by Brick as the level of work diminishes.

2.5 The report also recommends that, in parallel with the above that a sale for the Company should be considered and a final decision on sale or build out be made at a future meeting of the Cabinet.

3. THE REVIEW

Background

3.1 The Cabinet at its meeting on 25th November 2020, received a report on a strategic review by PwC of the Council's group of companies and other entities.

As a result of that review a number of specific recommendations were made concerning Brick by Brick.

These were to:

i) Authorise the initial further work required on the options identified by PWC regarding the Council's interest in Brick by Brick in order to best inform further consideration and decision at the January Cabinet meeting.

ii) Agree that funding of Brick by Brick shall continue in line with current loan arrangements and conditions subject to that further decision, provided that all funding for construction, and completed unit purchases be reviewed on a site by site basis.

iii) Agree that all site transfers to Brick by Brick, be halted until the Council has completed the options appraisal and taken a final decision on the options.

The level of work required as part of the second stage review was such that meeting the January report date was not practicable and it was agreed to move to the February Cabinet meeting. This was reported to the Scrutiny and Overview Committee at its meeting on December 21st 2020.

3.2 The Council has also received and agreed a number of recommendations regarding Brick by Brick in the Report in the Public Interest report by Grant Thornton. In particular that report contained four specific recommendations regarding the Council's future relationship with Brick by Brick. These were –

i) The Cabinet and Council should reconsider the financial business case for continuing to invest in Brick by Brick before agreeing any further borrowing.

ii) The Cabinet and Council should review and reconsider the ongoing financial rationale for the Council in the equity investment arrangement with Brick by Brick.

iii) The s151 officer and monitoring officer should monitor compliance with loan covenants with Brick by Brick and report any breaches to Members.

iv) The Cabinet and Council should review its arrangements to govern its interest in subsidiaries, how the subsidiaries are linked, the long-term impact of the subsidiaries on the Council's financial position and how the Council's and taxpayers interest is safeguarded.

These issues with regard to the Council's financial position are addressed in respect of Brick By Brick in this report (the wider governance considerations referred to at iv above are ongoing).

3.3 The initial strategic review commissioned by the September 2020 Cabinet covered a wide range of actions concerning not only Brick by Brick, but also Croydon Affordable Homes LLP and its group companies, Growth Zone, Revolving Investment Fund and Asset Investment Fund.

The resulting action plan was reported to the Scrutiny and Overview Committee on December 21st 2020, whose comments then were reported to Cabinet on 18th January. The action plan will be monitored under corporate arrangements as part of the Croydon Renewal Improvement Plan and, except where it specifically relates to the future options for Brick by Brick, is not referenced in this report.

Risk Appetite

3.4 Before examining the options available to the Council in regard to the future of Brick by Brick, it is essential that the Cabinet considers its current appetite for risk on investment activity with particular regard to the financial position that it finds itself in – i.e. a S114 notice and December 2020 submission to MHCLG for a capitalisation direction (loan) of £150m over 2020 - 2024.

When the Council set up Brick by Brick, there was limited regard evidenced in the Cabinet papers at the time of the potential downsides from investing through a wholly owned housing subsidiary and the risk to returns to the Council within a set period.

The emphasis in reporting the arrangements at that time was on the potential positives arising from the establishment of Brick by Brick with limited assessments of the risks potentially involved. The impact of that approach has in part led to the financial position that the Council now finds itself in. The Council now has significantly less scope for adopting investment proposals where an element of risk may lead to greater reward. The contrary argument applies that the greater risk may also lead to greater losses, so this is something the Council in its current financial position cannot afford to do.

This constrains some of the options available on the future of Brick by Brick, as albeit some of those options have a potentially greater reward, they also have a higher element of downside risk which could lead to increased losses.

In the light of this, the examination of the options has concentrated on where the Council can have greater certainty of outcome both in terms of future costs but also in terms of future income. The recommendations to Cabinet reflect this risk appetite.

Examining the Options

3.5 The November Cabinet report, stated that there were a range of options available to the Council ranging from closing Brick by Brick, to building out schemes on site, to selling off the business or maintaining the company and continuing the business as usual.

In order to inform the second stage of the report, the Cabinet agreed to procure assistance from a local firm of cost consultants (FFT) who examined a number of existing Brick by Brick schemes to gain a view as to the likely level of build costs on a range of their schemes, likely completion dates and indicative cash flows. Separately, valuation advice has been obtained on indicative sales figures for the same schemes.

These have been checked against information from Brick by Brick and then modelled by PwC to produce, in the absence of reliable cash flow data from Brick by Brick, some indicative cash flows for the immediate future to give some indication on two issues which are central to the consideration of future options for the company. Those two issues being:

(i) When the Council might start to receive repayment of some of its investment in Brick by Brick?

and

(ii) Whether the Council would need to make any short term cash injections to ensure that Brick by Brick remains solvent?

The resultant PwC report with recommendations is attached as Appendix 1 (but to the confidential part of the agenda only)

3.6 Before considering the benefits and disbenefits of the various options, it is important to note the stages of development of the various schemes undertaken by Brick by Brick. As at 1st January 2021, Brick by Brick had 29 schemes on sites transferred or under contract with 931 homes being built or completed awaiting disposal (i.e. awaiting sale to members of the public, RSL's or the Council).

Of that number 429 homes are likely to be completed by the end of October 2021, of the remaining 502 homes, completion is estimated to be concluded by Mid 2023

The list of schemes included in the above totals are shown in Appendix 2 and includes some sites where contracts have been let but part or all of the site hasn't been transferred to Brick by Brick or there are other issues to be resolved.

The latter schemes could be terminated and are referred to in Part B of this agenda.

It is assumed that for those schemes where a contractual commitment has **not** yet been made by Brick by Brick and where the land has **not** been transferred, development works will **not** be commenced and the potential future of these sites is referred to later in this paper. This is in accordance with the decision taken by Cabinet on 25th November 2020.

3.7 The benefits and disbenefits of the options outlined in the original PwC report are set out in Appendix 3.

Some of the options such as immediate closure, management buy out or "business as usual" are non-viable, due either to the size of the loss for the Council that would be incurred or the lack of substantive funding from the

Council to fund open-ended ongoing business other than for the immediate future.

The other options which involve either build out of sites, starting new sites or sale of the business all have an element of risk in terms of both valuation and cost uncertainty. This makes them potentially unpalatable options to the Council as the extensive build out would involve the Council entering into further General fund borrowing which would place additional pressures on the revenue budget without a guarantee of return.

The level of cost uncertainty and valuation assumptions are in the paper within the Part B of this agenda.

The decision as to which option to follow has been further narrowed by the proposal by the board of Brick by Brick not to build out 40 sites, which were under previous arrangements due to be transferred from the Council to Brick by Brick. This leaves the Council with the limited build out option of those 29 sites either transferred or under contract. Or a possible sale of the business based on the purchaser acquiring the Company which would include the ability to buildout the 29 sites in line with the existing planning consents.

This limited build out option (Scenario 1 in the Part B agenda) has merit as a considerable number of the sites are due to completed by the end of 2021 meaning that the Council is able to determine, with a degree of accuracy, the level of costs and income accruing to Brick by Brick and thus any residual income returning to the Council. It should be noted that Covid 19 restrictions could adversely impact completion dates and thus sales income as well potentially increasing costs.

3.8 However, the Scenario 1 option is not without issues as to build out all the sites, including some of the larger sites, means that Brick By Brick would have to continue as a trading entity to the end of this and the next financial year and into 2023/4. This has a number of inherent risks both in terms of cost and value but also in the practicality of keeping the company operational whilst it goes through what would, in effect, be a managed wind down.

A variant option (Scenario 2) has therefore been considered of a disposal and novation of some of the building contracts that would reduce Brick by Brick's, and thus the Council's, exposure to ongoing liabilities. This would involve the build out of the sites whilst purchasers were found for those sites that are not due to complete by October 2021. For Scenario 2 to be successful there would need to be a successful purchase arrangement from one or more bidders for the sites. On balance, this could be seen as a less risky alternative than a managed wind down and long build out and, as such, it may be more likely to maximise value to the Council. A sale to a single bidder could also involve the transfer of some Brick by Brick staff under the TUPE regulations.

3.9 Scenario 2 would require the full co-operation and agreement of Brick by Brick, initial discussions with the directors of Brick by Brick have been supportive of this approach. The arrangements, as set out in the Articles of Association and shareholder reserved matters, are that asset disposal would normally be a matter for Brick by Brick to determine where this is in line with the Cabinet approved business plan. The current business plan does not envisage this course of action and under the shareholder reserved matters this becomes a shareholder decision until such time as it is incorporated into an approved business plan.

In the light of this, Cabinet (if this option is agreed) would need to exercise its functions as shareholder to instruct and authorise the directors of Brick by Brick to commence a marketing exercise to sell onto other developers those sites that are not due to complete by the end of 2021.

The results of that exercise would then need to be reported back to the Council in order to allow the Council the opportunity to consider whether continued development of the site through Brick by Brick or the Council would be more cost effective than any offers received. The Council would then need to confirm whether they object to any disposal of the sites.

This disposal process would likely require decisions to be made swiftly and within timescales outside the normal Cabinet meeting timetable. It is therefore further recommended that, in order to ensure disposals are not jeopardised, decisions on whether to object to a disposal be made by the Interim Chief Executive in consultation with the section 151 officer and the Leader and subsequently be reported to Cabinet.

3.10 The decision to build out existing sites substantially under construction still has risk as Brick by Brick will effectively be in a “managed run down” situation and key staff may decide to leave, making it more difficult to manage the completion on site of those schemes. The Council and the board of Brick by Brick will therefore need to carefully monitor the situation and make arrangements to ensure that quick and speedy decisions can be made in order to minimise the Council’s exposure to additional financial risk. This may include authorising the board to dispose of further sites (other than those that are due to complete after October 2021) outside of the current authorised business plan, in circumstances where that is the most economically advantageous situation for the Council. In this case, again due to the likely need for emergency or expeditious action, it is recommended that the matter be delegated to the Interim Chief Executive in consultation with the Section 151 Officer and the Leader and subsequently be reported to Cabinet.

3.11 The Council would normally expect to receive and consider a business plan for approval from Brick by Brick at this time for operations in 2021/22. Whilst the strategic review has been undertaken, Brick by Brick have not been able to undertake work on a business plan. Even in the circumstances set out in this report and in accordance with the Articles for Association, a Brick by Brick business plan is still required and will need to include the arrangements set out in this report, in particular the arrangements for disposal of sites and the consequential impact on staffing and other related matters. This will be reported to a future meeting of Cabinet (by no later than May).

3.12 The other potentially viable option as set out in the Part B agenda could be a sale of the whole business to a third party. This option is under the PwC analysis potentially beneficial to the Council and would be at the choice of the Council not Brick by Brick. The initial view in November was that this option would both be time consuming and unlikely to be attractive to the market if the Council went into an open market situation. However, an off market sale would be less time consuming and could potentially generate a better outcome financially than the build out option. The Council has had one approach from an interested party and it is suggested that this be followed up to see on what terms a disposal might be possible and to compare those terms with the two scenarios contained in this paper. It should be noted that in the sale option and both of the scenarios the expectation is that the sites will be developed in terms of the mix of properties between private sale and affordable units (both social housing and shared ownership) contained in the planning consent. As explained in the Part B paper the Council would need to undertake due diligence on this offer. Please note the further resourcing required, as set out in section 6.

Other issues

3.13 **Funding Agreements**-The Council has as at 31st December 2020 lent £196, 287,521 to Brick By Brick. This excludes accrued interest of £27,300,023 that will be accrued by the end of the 20/21. A significant proportion of this sum, as identified in the original strategic review report, is in loans that are either time expired or not fully documented. As identified in both the strategic review report and the report in the public interest, these agreements need to be regularised. The original agreements were on the basis that loans effectively made up 75% of the value of the cash to be paid over to Brick by Brick with the remaining 25% being equity. The Council has never made any equity payments and is now not in a financial position to do so. The original loan agreements also specified that any sales proceeds from properties sold by Brick by Brick are placed in an account for the Council to apply to interest repayment and, if there is any excess, to substantive loan repayment. This process hasn't happened and sale proceeds have remained with Brick by Brick, in effect acting as working Capital replacing the Council's equity share. The Council needs to either regularise this arrangement, make variations to the current agreements or replace it with either fresh loans or equity.

3.14 The option of inserting equity is not feasible in the Council's current financial predicament and raising fresh loans would in effect only recycle the sales proceeds. However, the present arrangement as set out in the loan agreements, if properly exercised, does give the Council control and it is therefore recommended that the current arrangements continue but in a modified way to give Brick by Brick capacity to have working capital to ensure that funds are available to build out units on site. It should be noted that the PwC analysis assumes that sale proceeds are recycled to Brick by Brick until there is positive cash flow. There is a minimal requirement based on the PwC modelling below £10 million, which is supported by cash flow modelling from Brick by Brick and, as such, Cabinet is recommended to agree this further funding to Brick By Brick in relation to schemes proposed to continue with development (recommendation 1.2).

3.15 All of the loan agreements will need to be restructured or revised to cover the fact that there is now no equity input and the arrangements for working capital are covered as set out above. Discussions with the Council's legal advisors are ongoing as to whether this is best undertaken through a single overarching agreement or a series of site specific agreements with one to cover working capital. In any event, identified breaches explained above will be formally documented and addressed in accordance with recommendation 19 of the Report in the Public Interest. It is therefore recommended that decisions regarding any revision of the loan arrangements be delegated to the Interim Chief Executive in consultation with the Section 151 Officer and Monitoring Officer , the Leader , Deputy Leader and the Cabinet Member for Resources and Financial Governance. (as set out in recommendation 1.2).

3.16 **Fairfield Halls and the College Green site**
The refurbishment of Fairfield Halls was undertaken under license by Brick by Brick, as per the June 2016 decision of Cabinet. The initial intention was that these works would be at nil cost to the Council as the costs would be recovered by Brick by Brick from the profits on the sale of housing units from the adjacent College Green site. The Council has not, however, formally transferred the adjacent site to Brick by Brick. The arrangements concerning the governance and funding of this scheme are currently subject to a separate value for money investigation being undertaken by Grant Thornton as reported to members at the Scrutiny and Overview Committee in December 2020. The Council has, to date, lent in excess of £59 million to Brick by Brick to cover both the refurbishment of the halls and the planning costs of the adjacent site.

3.17 The estimated costs and values of developing the consented scheme on the College Green site have been checked by appointed consultants and officers are of the view that there is a viable scheme. However, the scheme will not generate sufficient resources to pay back the loan to date on the refurbishment and would require additional significant equity or loan amounts in excess of the current loan if the Council were to continue to undertake the scheme via Brick by Brick.

In addition, the Council would vicariously have both cost and value risk on a scheme that will take a number of years to complete. In the light of this risk and the additional short term borrowing involved, it is recommended that the College Green scheme, including elements of the adjacent car park, is not progressed by Brick by Brick. It is also recommended that the Council undertake a procurement exercise (in accordance with the Council's Tenders and Contracts Regulations) to appoint marketing agents to report back to Cabinet on the best options for the disposal of the College Green site, including the adjacent car park (recommendation 1.4). This further report will also take cognisance of the findings of the Grant Thornton value for money review.

3.18 **Future of sites not transferred to Brick by Brick.** There are four sites where the Council has not yet transferred land where Brick by Brick have either commenced work on site or have effectively entered into a contract to commence building. These sites are detailed on the Part B paper. As part of the detailed analysis, it is recommended that the previous plans to transfer these sites to Brick By Brick continue and then be included in the marketing exercise referred to in para 3.9, which would then potentially be transferred to any eventual developer.

3.19 The Council has previously agreed to transfer a number of sites to Brick by Brick. These sites are at various stages in the planning process ranging from feasibility, through to obtaining planning consent. The known list of sites which were previously agreed to transfer are detailed in Appendix 4. This list may be incomplete .

The Council has lent £1,371 million to Brick by Brick in specific loans developing these sites, and part of the £35.265 million on development cost loans will also be attributable to these sites.There is potential to either sell on the sites or develop these for social housing within the Housing Revenue Account (although, at present, the value of this work is unquantifiable). However, that value will accrue to the Council at some future stage and it will need to recognise that the loans made to Brick by Brick for this work will now, like those for Fairfield Halls, need to be treated as a potential bad debt.

With regard to the sites set out in Appendix 4, the Council will need to decide on a site by site basis whether to retain or dispose of the site or to follow through with planning consents to maximise potential value to the Council. It is therefore recommended that the sites identified in Appendix 4 be subject to a further report back to Cabinet on their future use (recommendation 1.5). It should be noted that a number of sites that currently have planning consents subject to confirmation of section 106 agreements are likely to lapse as they are close to being time expired and the consents may not now be in accordance with planning policy.

Resources will need to be identified from within the Council to undertake this work both from within the property services team as well as the planning service.

3.20 **FUTURE DELIVERY OF SOCIAL HOUSING**. Brick by Brick was originally set up to provide a vehicle by which the Council was able to meet housing demand, in particular affordable housing for rent at a time when there were constraints on the Council's ability to provide such housing through direct delivery via the Housing Revenue Account (HRA). The abolition of that constraint, namely the HRA borrowing cap in 2018, meant that the Council has, since 2018, been able to directly deliver new social housing subject to the constraint of affordability within the HRA.

3.21 The Council, however, chose to continue to deliver new social housing units through Brick by Brick. If the Council decides that it no longer wishes to deliver housing via Brick by Brick and it wishes to provide additional affordable rented accommodation through the HRA, it will need to establish processes to both identify schemes that are physically capable of being developed in planning and construction terms but are also financially viable, in that the rent charged covers the revenue costs of managing and maintaining the new stock as well as the cost of funding any borrowing.

It should be noted that a revised policy on rent setting across the new build units is considered elsewhere on this Cabinet agenda .That policy, if approved, will assist with scheme development viability, including those schemes which are potential acquisitions from Brick by Brick into the HRA. In the event that some of those schemes are not viable, even within the parameters of the proposed rent policy, the Council may have to return GLA grant and/or lose the ability to recycle Right To Buy (RTB) receipts within the required time limits.

3.22 A number of the sites in Appendix 4 could potentially fall into that category, particularly those that are currently on HRA land, utilising the existing work from Brick by Brick, high level appraisals will be undertaken on the delivery of social housing on those sites and reported back to Cabinet as part of the HRA Business Plan.

3.23 The Council has previously agreed to purchase a number of completed units for social housing purposes within the HRA. These purchases were put on hold as part of the November 2020 Cabinet report. These sites are indicated in Appendix 2 and could result in up to 187 additional social housing units . On a site by site basis, where units meet the revenue affordability criteria set out in para 3.21 (i.e. that rent covers operational and financing costs and that the price agreed for purchase is deemed to be at market levels) purchases will be confirmed with Brick by Brick and payment be made on completion . A number of the sites in the July 2020 paper were originally designated as shared ownership , it is possible that Brick by Brick may receive better financial offers in respect of these units as shared ownership units in that case it is possible that those sites will be sold as shared ownership units to a registered provider rather than as social housing to the Council.

4. CONSULTATION

4.1 No formal consultation has been made on this report, other than factual accuracy checks with external third parties. Consultation on the future use of sites will need to take place in line with the council's normal arrangements.

5. PRE-DECISION SCRUTINY

5.1 This report was submitted to the Scrutiny and Overview Committee for comment at its meeting on February 9th 2021.

6 FINANCIAL AND RISK ASSESSMENT CONSIDERATIONS

6.1 This report considers the various proposals in regards to future operations of Brick by Brick. The recommended course of action involves allowing Brick by Brick to continue building out schemes at an advanced stage, reviewing sites no longer proposed for development, disposing of sites at intermediate stage or sell the shares of the Company. The impacts of each is described in Section 6.5 below.

6.2 The option to sale the business will be worked on in parallel to the other proposals. Whilst the sale option can be worked in parallel for some time, there will come a point when the Council will need to decide if it wants to continue with disposing of sites or sell the Business.

6.3 It is important to note that all funding provided by the Council has been provided through the Council taking on borrowing and then on lending this to Brick by Brick at a margin. The Council currently does not provide minimum revenue provision (MRP) on its loans to Brick by Brick due to the short nature of the loan period. However, as part of the 2021/22 Budget Setting report and the Treasury Management Strategy (to be reported to Full Council on 8th March 2021) the Council will revise its policy to ensure the most prudent approach is taken on any funding provided to Brick by Brick.

6.4 **Option to continue development of schemes within the Brick by Brick with completion date of October 2021.** There are 20 schemes that are planned to continue within Brick by Brick (Appendix 2). In order to complete the schemes the current loan agreement will be extended and additional loan funding will be provided so that the Council now lends 100% of the development costs through debt financing. In order to lend the money to Brick by Brick the council will need to borrow the funds from Public Works Loan Board (PWLB) and on lend to Brick by Brick at a margin. This is recommended to be at a maximum of £9.99 million.

6.5 Whilst the Council does not have sighting of the scheme viability the expectation is that once these schemes are developed and the residential units sold, that will provide sufficient receipts to Brick by Brick to pay back the debt and interest income.
There is a risk that if Brick by Brick does not receive sufficient receipts from the disposal then the Council will not receive its funding back. This will require the Council write off the remaining loan balance and to carry cost of the loans.

6.6 **Option for Disposal of developments directly from Brick by Brick with completion date beyond October 2021**. There are 9 schemes (Appendix 2) that are planned to be disposed of by Brick by Brick. In this option the Council will not be providing further funding however once developments are disposed of by Brick by Brick it is expected that the company will use the receipts to pay back the outstanding loans. Should Brick by Brick not receive sufficient receipts from the disposals of its developments the Council will have to write off any outstanding loans balances and incur financing costs.

6.7 **Options for Disposal of College Green Site from the Council.** The Council has lent £1.7m to Brick by Brick to carry out various development works at the College Green Site. When the site has been disposed of the receipts will be used to payback the outstanding Brick by Brick loan regarding this site. As in the other two options the risk is that should sufficient receipts from the disposal not be realised the Council will have to carry the cost of financing the outstanding loan amount.

6.8 As the report indicates this option has inherent risks due to poor governance and funding arrangements and therefore detailed financial implications will be provided once the review from Grant Thornton has been completed.

6.9 **Option to Review remaining sites.** Financial implications will be explored once the review has been completed of the schemes identified in Appendix 4. If the proposal is to bring developments back into the Council then all loans related to those schemes may need to be written off in the first instance. This will create an ongoing financing charge, through provision of the MRP, until that debt can be paid back. The Council will need to carry out an accounting assessment and seek advice from Treasury advisors if sites are being passed onto the HRA.

6.10 **Sale of the Company (Share Sale).** This option will require significant due diligence and assessment against other options detailed within 6.4 to 6.9, before a definite financial implication analysis can be provided. The final assessment will depend upon the offer from a potential bidder and how the transactions are arranged to ensure the Council can recoup its loans to the Company. The Council will also need to incur additional costs to support the share sale option (to be progressed in accordance with the Council's Tenders and Contracts Regulations and Spend Control Panel procedures) and shall be updated as part of the monthly financial performance reports.

6.11 In addition Brick by Brick has various staff who are part of the Council's Local Government Pension Scheme. Depending on the outcome of the work being done to review Brick by Brick, there will be impact on staffing within the company. Should staff decide to leave the company they will have option to either maintain their pension benefits or may seek to exit their membership and pass the benefits to another scheme. However, depending on their age staff may also be able to cash in on their pension earlier which will mean the Council's pension fund will need to make benefit payments.

Approved by: Lisa Taylor, Director of Finance Investment and Risk.

7. LEGAL CONSIDERATIONS

7.1 The Head of Commercial and Property Law comments on behalf of the Director of Law & Governance that under the Council's general power pursuant to Section 1 of the Localism Act 2011, the Council may exercise its rights as sole shareholder of Brick by Brick Croydon Ltd to take the steps identified in this report. Under the Articles of the company, the matters addressed are within the scope of "reserved matters", i.e. matters for which the company needs shareholder approval and where the Council (as shareholder) may direct the company (and its directors).

7.2 In making decisions under this report, Members will need to be mindful of the Council's financial position (including under the Section 114 notice), its fiduciary duties and the requirement to have regard to all relevant factors and to disregard irrelevant ones. The Council must act in accordance with the principles of Wednesbury reasonableness, meaning decisions that a rational person might make, having regard to all relevant considerations.

7.3 In relation to the recommendations in respect of revised funding arrangements, external legal advice from Browne Jacobson LLP has confirmed that this gives rise to no breach of the new "Subsidy Control "regime (formerly State aid). This is on the basis that the Council is acting as a rational private-sector party would act (being sole shareholder and lender), and having taken financial advice identifying options that such a private sector party would rely on (i.e. focussed on how the Council may best recover the investment made to date alongside other relevant considerations such as the risks and timings involved).

7.4 Further advice may be required regarding the self-delivery (and acquisition) options referred to in paragraphs 3.20 to 3.23, insofar as decisions relate to the powers of the Council under housing law, including in relation to HRA accounting.

Approved by Sean Murphy, Head of Commercial and Property Law & Deputy Monitoring Officer on behalf of the Interim Director of Law & Governance.

8. HUMAN RESOURCES IMPACT

8.1 There are no HR implications or impact for the Council as a result of this report; and if any arise these will be managed under Brick by Brick, policies and procedures as staff group are directly employed under Brick by Brick terms and conditions.

Approved by Jennifer Sankar, for and on behalf, of Sue Moorman, HR Director.

9. EQUALITIES IMPACT

9.1 There are no equalities impacts arising from this report. However the implications of the issues raised and how they are addressed may have an effect on the medium term financial plan. Any subsequent savings plans that have a staffing impact or impact on vulnerable and/or groups that share a protected characteristic will be subject to agreed HR procedures, formal consultation and equality analysis.

Approved by: Yvonne Okiyo, Equalities Manager

10. ENVIRONMENTAL IMPACT

10.1 There are no environmental impacts arising from this report

11. CRIME AND DISORDER REDUCTION IMPACT

11.1 There are no Crime and disorder reduction impacts arising from this report

12. REASONS FOR RECOMMENDATIONS/PROPOSED DECISION

12.1 There is no ideal option in dealing with Brick by Brick, all of the options and scenarios reviewed have a mix of risks and costs in the form of debt write off attached to them. However, taking into account the Council's financial situation and the level of risk involved in a number of the options, the option to either build out sites and subsequently sell some of them or sell the business are the only options that reduce risk whilst minimising the level of debt write off to the Council. None of the options are without some cost write off but the Options to be taken forward in this paper for further consideration whilst a potential sale is considered reduces the risk of write off.

13. OPTIONS CONSIDERED AND REJECTED

13.1 The report contains a range of options considered by the PwC strategic review report issued initially in November and now concluded. These are outlined in the body of this report in the attached appendix 3, and the confidential paper. Financial analysis and the Council's necessary lowered risk appetite and financial capacity means that the other options considered presented greater financial risk to the Council and as such were unviable. However, the viable options as set out in this paper can be investigated in parallel so that the Council is in a position to make a firm decision on build out or sale once due diligence has been undertaken by and on the prospective purchaser.

14. DATA PROTECTION IMPLICATIONS

14.1 **WILL THE SUBJECT OF THE REPORT INVOLVE THE PROCESSING OF 'PERSONAL DATA'?**

NO

14.2 **HAS A DATA PROTECTION IMPACT ASSESSMENT (DPIA) BEEN COMPLETED?**

NO

CONTACT OFFICER: Chris Buss, consultant

APPENDICES TO THIS REPORT:
Appendix 1 – PwC Report (Part B agenda)
Appendix 2 – Schemes under construction
Appendix 3 – Options for future of Brick by Brick
Appendix 4 – Sites awaiting transfer to Brick by Brick

BACKGROUND DOCUMENTS: None