



To all Members of the Policy and Resources Cabinet Committee

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Date: 27 April 2022

Dear Member,

POLICY AND RESOURCES CABINET COMMITTEE - WEDNESDAY, 4 MAY 2022

I am now able to enclose, for consideration at next Wednesday's meeting of the Policy and Resources Cabinet Committee, the following report(s), which were unavailable when the agenda was printed.

Agenda Item No

4 **Minutes of the meeting held on 24 March - TO FOLLOW** (Pages 1 - 10)

5 **Inflationary Pressures on Capital Construction Programmes - TO FOLLOW** (Pages 11 - 22)

Yours sincerely

A handwritten signature in black ink, appearing to read 'Ben Watts', is written over a faint circular stamp.

Benjamin Watts
General Counsel

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KENT COUNTY COUNCIL

POLICY AND RESOURCES CABINET COMMITTEE

MINUTES of a meeting of the Policy and Resources Cabinet Committee held in the Council Chamber, Sessions House, County Hall, Maidstone on Thursday, 24 March 2022

PRESENT: Mr R J Thomas (Chair), Mr N Baker (Substitute for the Conservative Vacancy), Mr P V Barrington-King, Mr P Bartlett, Mr A Brady, Mr N J D Chard, Mr M Dendor, Mr A J Hook, Mr R C Love, OBE, Mr J P McInroy, Mr H Rayner (Substitute for Mr T Bond), Mr P Stepto and Dr L Sullivan

ALSO PRESENT: Mr R W Gough and Mr P J Oakford

IN ATTENDANCE: Mrs A Beer (Corporate Director of People and Communications), Mr D Cockburn (Corporate Director Strategic & Corporate Services), Ms Z Cooke (Corporate Director of Finance), Mr S Dodd (Investment and Development Consultant), Ms L Gannon (Director of Technology), Mr V Godfrey (Director, Kent Holdco Ltd), Mr D Lindsay (Interim Head of Technology Commissioning and Strategy), Ms C Maynard (Head of Commissioning Portfolio - Outcome 2 and 3), Ms K Ripley (Special Projects Manager), Mr J Sanderson (Head of Property Operations), Mr M Scrivener (Corporate Risk Manager), Mrs R Spore (Director of Infrastructure), Mr B Watts (General Counsel), Mr D Whittle (Director of Strategy, Policy, Relationships and Corporate Assurance), Mr C Wimhurst (Commissioning Standards Manager), Mr J Cook (Democratic Services Manager) and Miss T A Grayell (Democratic Services Officer)

UNRESTRICTED ITEMS

60. Apologies and Substitutes

(Item 2)

Apologies for absence had been received from Mr T Bond, Mr T Cannon, Mr G Cooke and Mr P C Cooper.

Mr N Baker was present as a substitute for Mr Cannon and Mr H Rayner as a substitute for Mr Bond.

The committee noted that Mr P Barrington-King, Mr N J D Chard and Mr A J Hook were joining the meeting remotely.

61. Declarations of Interest by Members in items on the Agenda

(Item 3)

In relation to agenda item 12, the Chair declared that, as a former pupil of the Simon Langton Grammar School for Boys, he made voluntary monthly contributions to the school's funds.

Mr N Baker declared that he was also a former pupil of the school, and that his fiancée was employed by the East Kent Hospitals University NHS Foundation Trust.

In relation to agenda items 8 and 9, Mr H Rayner declared that he held shares in the Kier group of companies.

62. Minutes of the meetings held on 19 January and 22 February 2022
(Item 4)

It was RESOLVED that the minutes of the meetings held on 19 January and 22 February 2022 are correctly recorded and they be signed by the Chair. There were no matters arising.

63. Risk Management: Strategic and Corporate Services
(Item 5)

1. The Leader of the County Council, Mr R W Gough, introduced the report and highlighted the impact of various factors, including the impact on the supply chain of the conflict in Ukraine. Mr Gough, Mr Whittle and Mr Scrivener responded to comments from the committee, including the following:-

- a) asked what proactive measures could be put in place to support the wellbeing of staff who were working with covid, Mrs Beer advise that many staff testing positive for covid were able to work effectively, remotely, if they had only mild or no symptoms. Staff were always encouraged to schedule regular breaks away from a computer screen, preferably in fresh air, as this had been proven to protect wellbeing as well as boost productivity. The onus of supporting staff's physical and mental wellbeing was on line management, who were expected to check regularly that staff were managing their workload effectively. She assured Members that staff working through covid had chosen to do so but were not expected to do so;
- b) asked how frontline staff who worked with the public, for example, in Adult Social Care roles, would be supported, Mrs Beer assured Members that such staff would not be expected to engage with the public while unwell;
- c) asked about the resilience of the Council's technology and information security, Mr Whittle undertook to provide more information on this to Members following the meeting. Mr Gough added that the Council was unable, realistically, to mitigate all risks but was proactive in doing whatever it could;
- d) a view was expressed that the largest area of risk in terms of information security was human error; and
- e) it was emphasised that many risks related to more than one directorate; the actions of one directorate would affect the work of another.

2. It was RESOLVED that the information set out in the report and given in response to comments and questions be noted, with thanks.

64. Update from the Contract Management Review Group (CMRG)

(Item 6)

1. Mr Oakford and Mr Wimhurst introduced the report and set out the aims of the restarted review group in assuring good practice. The new contract management mechanism used by the group would help bring together and manage all commissioning activity in the future. Mr Wimhurst and Ms Maynard responded to comments and questions from the committee, including the following:-
 - a) the new register of contracts was welcomed and a request made for this to be shared with Members of the committee. Mr Wimhurst undertook to do this;
 - b) asked if re-procurement costings could be included in future reporting, Ms Maynard assured the committee that this would be done; and
 - c) the restart of the group was welcomed, and work to share more information with Members would increase accountability.
2. It was RESOLVED that the information set out in the report and given in response to comments and questions be noted, with thanks.

65. Work Programme 2022

(Item 7)

It was RESOLVED that the committee's planned work programme for 2022 be agreed.

66. Consideration of exempt content

(Item)

The Chair asked the committee if they wished to refer to the exempt information included in the appendices for the following items. Members confirmed that they did not wish to and, accordingly, the discussion of items 8, 9 and 11 took place in open session.

Item 10 was discussed in closed session.

67. Implementing a new Facilities Management Model

(Item 8)

Mr H Rayner declared that he held shares in the Kier group of companies but remained in the meeting for item 8.

1. Ms Ripley introduced the report, about which there were no questions or comments.
2. It was RESOLVED that the decision proposed to be taken by the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, to:

- a) adopt and implement a new Facilities Management Model, with one hard facilities management services contract and series of soft services contracts, as set out within the exempt report; and
 - b) delegate authority to the Director of Infrastructure, in consultation with the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, to finalise, agree, award and enter into contracts, following the procurement process, to deliver the new Facilities Management Model,
- be endorsed.

68. Construction Partnership Framework Commission
(Item 9)

Mr Rayner left the meeting for this item, having previously declared an interest.

1. Mr Sanderson introduced the report and highlighted the new model and process for procurement. The framework would be initially for four years with a potential extension for two years and would apply to projects with a value of over £1million. He responded to comments and questions from the committee, including the following:-

- a) of the 13 organisations selected to tender, 11 were Kent-based companies or had offices within Kent;
- b) clauses within the framework contract required suppliers to actively use small and medium and local businesses, as well as taking reasonable steps to offer opportunities to supported businesses;
- c) to ensure that companies, particularly smaller ones, were able to benefit fully from being involved, the framework agreement required the supplier to ensure that payments to the supply chain were made within 30 days of receipt of application/invoice;
- d) the list of quality criteria in the report included social value low down but Members were assured that criteria were not presented in any order of priority. For example, environmental responsibility and social value was listed last but accounted for 25% of the overall quality weighting in the procurement assessment process; and
- e) contracts with a value of less than £1million were mainly delivered through the Total Facilities Management model. A new minor works partnership framework was being proposed and a separate report on this would be coming to a future meeting of the committee.

2. It was RESOLVED that the decision proposed to be taken by the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, to:-

- a) establish the Kent Construction Partnership Framework, to replace the Kent Contractors framework; and

- b) to authorise the Director of Infrastructure to enter into the necessary legal documents to establish the framework,

be endorsed.

69. Property Accommodation Strategy - Strategic Headquarters: Update and Next Steps March 2022

(Item 11)

1. Mr Oakford introduced the report and advised that the requirement to realise the capital meant that the Council was now committed to moving forward with plans, although the timetable for the project was not yet clear. Mrs Spore presented a series of slides which set out the options and plans for the different parts of the Sessions and Invicta House buildings. These included an artist's impressions of the proposed residential and business uses of Sessions House blocks A and B, respectively, and the Gensler model proposed for use in Invicta House. The Civic Centre of Sessions House, comprising blocks C and D, would include the Council Chamber, Member areas and group offices as well as housing the Corporate Management Team, Governance, Law and Democracy and meeting space. Logistics would be a major part of the project, and it was planned that work to Invicta House would need to be completed first before Sessions House could be started. Members, staff and meetings would need to be accommodated at other locations while the work was undertaken. The current planned completion date for the project was August 2024.

2. Mr Oakford and Mrs Spore then responded to comments and questions from the committee, including the following:-

- a) the retention of a civic function at Sessions House was welcomed;
- b) most speakers were happy to note the proposals at the current time but accepted that plans may have to change in the future. Mr Oakford emphasised the long-term nature of the project and that options such as relocation or purpose-building new premises had been examined and discarded, with a confirmed wish to stay in the county town and have premises fitting of a first-tier authority. Increased remote working arising from the pandemic had changed the need for staff accommodation. Funding had been committed to get the project to RIBA stage 3, at which time the next stage could be planned; and
- c) asked at what point repairs to the current premises would cease to be cost-effective, Mr Oakford assured the committee that he would not have committed to retain part of Sessions House as a civic centre if the Council could not afford the refurbishment costs. Some parts of Sessions House needed considerable maintenance expenditure, to remain operational, and the aim was to seek the most effective option available for the Council.

3. The Chair thanked Members for the good range of views expressed and thanked Mr Oakford for being open-minded in listening to the views expressed.

4. The committee RESOLVED to note:-

- a) the progress and revised design proposal for the refurbishment of both Invicta House and Sessions House blocks C and D;
- b) the intention to review the procurement strategy for engaging a main contractor in respect of the proposed works at Invicta House and Sessions House blocks C and D; and
- c) that a procurement process will commence to explore further the co-working opportunities focusing on block B and that a marketing process will commence in respect of blocks A/E and B, to seek a development partner.

Mr A Brady and Dr L Sullivan asked that their abstentions from this resolution be recorded in the minutes.

70. Motion to exclude the press and public for exempt business

(Item)

The committee RESOLVED that, under Section 100A of the Local Government Act 1972, the press and public be excluded from the meeting for the following business on the grounds that it involves the likely disclosure of exempt information as defined in paragraphs 3 and 5 of part 1 of Schedule 12A of the Act.

EXEMPT ITEMS

Open access to minutes 71, 72 and 73

Summary of minute 74
(where access to that minute remains restricted)

71. Annual Cyber Security Update

(Item 10)

1. Mr Oakford introduced Lisa Gannon, the new Head of Technology, to the committee and the Chair welcomed her to her first meeting. Ms Gannon introduced the report and, with Mr Lindsay, responded to comments and questions of detail from the committee, including the following areas:-

- a) managing the slightly higher risk associated with devices supplied by a third-party supplier, and the risk of staff printing material from home, the latter being an information governance rather than a technology issue;
- b) managing the reporting of suspicious emails, and what feedback is given to staff to encourage them to continue to report in the future;
- c) managing the issue of password strength against staff's ability to remember them, and achieving a balance between security and ease of access;
- d) asked if the figures listed in the report for the number of spam emails reported by staff included phishing emails, Mr Lindsay undertook to check and advise the speaker after the meeting; and

- e) asked how Kent County Council compared to other local authorities around the country in terms of cyber security, Ms Gannon advised that the Local Government Association collated such information from local authorities. She assured Members that Kent's systems were generally very sound.

2. Mr Watts advised that a report on Member IT issue was to be discussed shortly by the Selection and Member Services Committee, suggesting the establishment of a Member working group. Details of the group would be sent to all Members.

3. It was RESOLVED that the Council's current approach to cyber security be noted, with thanks.

72. 22/00031 - Strategic options for Langton Field, Canterbury: Land adjacent to Kent and Canterbury Hospital
(Item 12)

The Chair declared that, as a former pupil of the Simon Langton Grammar School for Boys, he made voluntary monthly contributions to the school's funds.

Mr N Baker declared that he was also a former pupil of the school, and that his fiancée was employed by the East Kent Hospitals University NHS Foundation Trust.

1. Mrs Spore and Mr Dodd introduced the report and advised that the procurement process was at an early stage and there was further consultation to be undertaken. The County Council was working closely with Canterbury City Council and the NHS to progress options. Of the three options set out in the exempt report, Option 2 was preferred as the simplest and the one on which the three parties were most likely to reach agreement.
2. In response to questions, Mrs Spore and Mr Dodd assured Members that any view expressed by the committee today would not influence any NHS plans for a new hospital development at the site but would form the basis for the County Council's future actions, if such plans should come to fruition. The process had already taken four years and was expected to take much longer.
3. The recreation and health value of open green space in Canterbury was emphasised.
4. Mr H Rayner proposed and Mr R Love seconded the recommendation set out in the exempt appendix B to the report; that, considering the analysis undertaken and advice received, Option 2 be progressed.
5. It was RESOLVED that the decision proposed to be taken by the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, to agree that the Director of Infrastructure, in consultation with the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, progress with Option 2 (as set out in the exempt appendix B to the report), finalise and enter into all necessary legal and other documentation with one or more parties to optimise Kent County Council's land holdings position at Langton Land, Canterbury.

Mr A Brady and Dr L Sullivan asked that their abstentions from this resolution be recorded in the minutes.

73. 22/00032 - Works at the Turner Contemporary Gallery, Margate
(Item 13)

1. Mr Oakford, Mrs Spore and Mr Sanderson introduced the report and responded to comments and questions of detail from the committee, including the lease arrangements for the building, the expected cost of the works and how this would be covered, and the element of financial risk to the County Council.
2. The committee then agreed the recommendation set out in the exempt report and RESOLVED that the decision proposed to be taken by the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services to agree to:
 - a) the required works at Turner Contemporary Gallery and related activity, as detailed in the exempt decision report; and
 - b) delegate authority to the Director of Infrastructure, in consultation with the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services, to take necessary actions, including but not limited to entering into contracts required to deliver the works,be endorsed.

74. Kent Holdco - Education Supplies
(Item 14)

1. Mr Oakford and Mr Godfrey introduced the report and responded to comments and questions of detail from the committee, including the legal requirement to comply with Public Contracts Regulations, the relationship between the County Council and the company, and accountability. The committee debated possible ways forward.
2. The committee then agreed the recommendation set out in the exempt report and RESOLVED that the decision proposed to be taken by the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services be endorsed.

Mr H Rayner and Mr P Bartlett did not support the recommendation and asked that their opposition to it be recorded in the minutes.

Mr A Brady and Dr L Sullivan asked that their abstentions from this resolution be recorded in the minutes.

By virtue of paragraph(s) 3 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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From: Peter Oakford, Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services

Rebecca Spore, Director of Infrastructure

To: Policy and Resources Cabinet Committee – 4 May 2022

Subject: Inflationary Pressures on Capital Construction Programmes

Key Decision: Expenditure or savings of more than £1m and affects more than 2 Electoral Divisions

Classification: UNRESTRICTED

Past Pathway of Paper: Not applicable

Future Pathway of Paper: Not applicable

Electoral Division: All

Summary: The national fiscal and economic context is an important consideration for the Council in setting and managing its revenue and capital budgets. The budget report to County Council on 10 February referred to the extraordinary and unexpected challenge to the UK economy and economies across the world arising from the COVID-19 pandemic. Kent County Council (KCC) has a significant Capital Construction Programme, which has been adversely impacted by the inflationary pressures facing the UK construction industry.

This report seeks to ensure that KCC has sufficient capital allocated and effective contractual management arrangements in place to deliver the programmes and projects, with anticipated additional costs as set out in the Medium Term Financial Plan. A decision is required to implement these in the time available to avoid disruption to front line services and to secure the contractual arrangements for the provision of key infrastructure projects, including the provision of school places to meet KCC's statutory duties.

Recommendation(s): The Policy and Resources Cabinet Committee is asked to consider and endorse or make recommendations to the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services on the proposed decision to:

1. note the £28.8 million estimated impact on capital budget spend in the Medium Term Financial Plan of £339.3 million across the capital programme for 2022-23, were already approved via key decision or covered by appropriate delegated authority to be funded from the options identified in paragraph 5.9 of this report;
2. consider the use of Fluctuation clauses when deemed necessary to control costs to KCC and alleviate adverse effects to the main contractor supplier of the rise in material costs; and
3. delegate authority to the Director of Infrastructure or for Highway Schemes the Corporate Director of Growth, Environment and Transport, in consultation with the Corporate Director of Finance, to take the necessary actions, including but not limited to entering into contracts and other necessary documentation to enable the delivery of the capital programme taking into account construction and inflation where existing Record of Decisions levels are needed to be adjusted.

1. Introduction

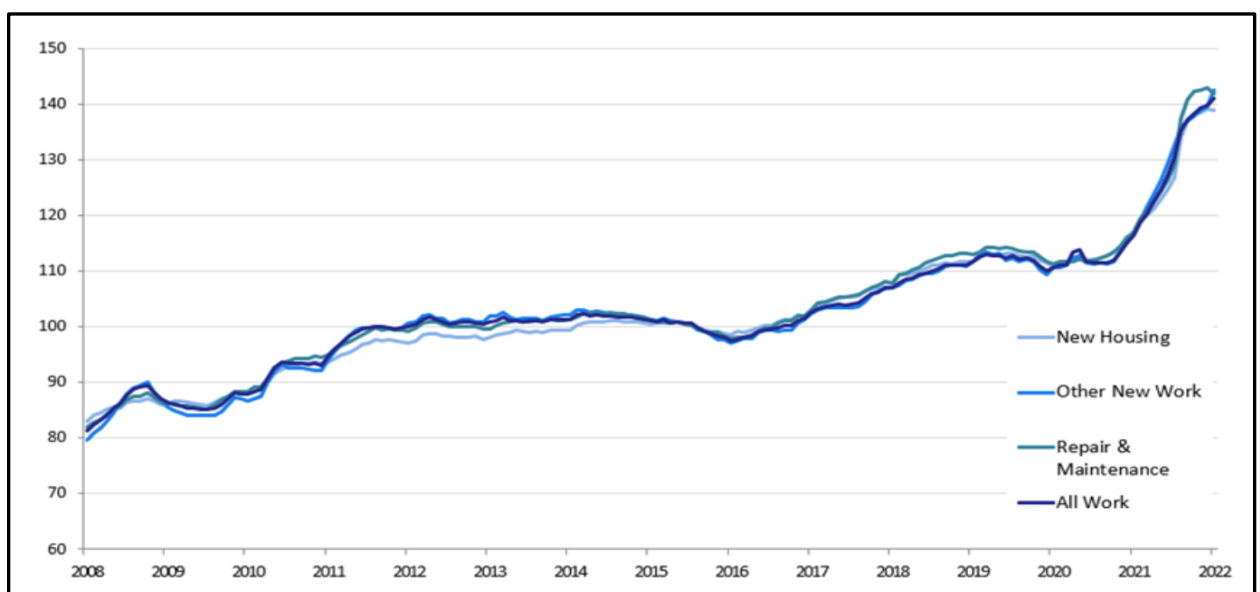
1.1. The construction industry, in the past year has experienced acute inflation pressures, long material lead times and sporadic material supply. This has been directly linked to material and labour shortages. The identified key causes of the shortages are the effects of:

- COVID-19 Pandemic on; the manufacturing industry; sudden increase in demand on the construction industry post the global lockdown and decreased supply chain due to administrations.
- Brexit on; supply of construction workers and hauliers to transport the construction material and complying with regulations.
- Changes in UK Government legislation and Building Regulations and requirement to meet Net Zero targets.
- Rising cost of wholesale energy.
- Indirect effects of the Russian invasion of Ukraine.

1.2. This report seeks to inform The Policy and Resources Cabinet Committee on the impact that cost inflation and the sporadic supply of materials has had, and will continue to have, on KCC's capital programme budgets and the delivery programme. The report will also suggest mitigation measures to assist in reducing the impact of the cost inflation where possible.

2. Current Position

2.1. Since the first quarter of 2021, The Department for Business, Energy, and Industrial Strategy (DfBEIS) are reporting that all sectors of work within construction experienced a 21% annual price rise on construction materials. The (DfBEIS) Graph 1 below shows an unprecedented sharp rise in the Construction Material Price Indices (CMPI) in the UK during 2021.



Graph 1 - Construction Material Price Indices, UK taken from DfBEIS Monthly Statistics of Building Materials and Components Commentary, February 2022.

2.2. The Building Cost Information Service (BCIS) Graph 2 below, shows the severity of the material price increases of key materials on construction projects from 1Q2021

to 3Q2021.



Graph 2 - Construction materials: Price Movement from 1Q2021 to 3Q2021 taken from BCIS news Construction materials cost increases reach 40-year high

2.3. Table 1 below shows construction materials experiencing the greatest price increases and decreases in 12 months from January 2021 to January 2022. The aggregated construction material price index hides larger price movements for some specific products and materials. The three largest increases and two decreases are presented.

Construction Materials	Year-on-year % change
Greatest price increases	
Fabricated structural steel	51.0
Particle board	45.4
Concrete reinforcing bars	40.0
Greatest price decreases	
Insulating materials (thermal and acoustic)	-3.3
Gravel, sand, clays & kaolin (including aggregate levy)	-3.3

Table 1: Construction materials experiencing the greatest price increases and decreases in 12 months to January 2022, UK

2.4. The data provided above does not consider the effects from the conflict in Ukraine. However, it is predicted that the war will have inflationary pressure on construction materials.

2.5. It is predicted that the direct impact of the conflict on material supply and cost in the UK is low as the total share of construction material imports from Russia, Ukraine and Belarus is less than 2%.

2.6. Indirectly the UK is likely to suffer shortages due to the sanctions via European

firms that form part of the UK supply chain (firms that produce construction materials that contain petro-carbons or consume copious amount of energy in manufacturing). These firms are heavily reliant on Russia for energy (Russia supplies 30% of Europe's oil and 35% of its natural gas). Some European firms also rely on Russia for supply of raw materials such as copper and timber. Once this supply source is removed, sourcing alternative suppliers may not be available or may be more expensive – as this involves brokering fresh deals which may cost more, this is still an unknown and cannot be forecast in this report.

- 2.7. The Contractors Leadership Council (CLC) are also reporting anticipating that the contractors current tender pricing strategies will become increasingly difficult to maintain, due to issues resulting from the Ukraine conflict which include, but are not limited to, inflation and supply chain instability. They expect that the longer the conflict continues the more severe the impact will be.
- 2.8. The level of uncertainty around the impact of the conflict has resulted in material suppliers being unwilling to hold their prices for 24 hours, which poses an issue for contractor's who are tendering, as they cannot provide a fixed price to the client, without risking making a loss when the true impact is realised.
- 2.9. The following non-financial mechanisms have been incorporated to support contractors who are already in contract with KCC:
 - Contractual Mechanisms – facilitating the early procurement of materials that can be purchased in advance and either stored on or off site.
 - Increased flexibility in material selection to allow options that were readily available at the time, with minimum impact on the quality of the build.
- 2.10. These supporting mechanisms have been vital to ensure that KCC contractors have had the required support, to enable them to deliver projects during the unprecedented crisis they faced during the summer months of 2021 (2Q2021 and 3Q2021). The contractors experienced a relatively stable period in 4Q2021, and this sentiment was echoed in the press. Nationally 4Q2021 was less volatile than the preceding quarters.
- 2.11. Material price increases will impact capital projects without construction contracts and are due to be procured. There are some projects that have already been procured but with long programmes and substantial variations or have programmes that have been extended or phased and still on site. These projects will also be affected.
- 2.12. The increase to input costs will be reflected in the tender returns that KCC will receive. The press is reporting that the main contractors have been absorbing some of the impact by reducing their profit margins to ensure construction projects are not shelved. However, CLC do not see this position continuing to support the rising fuel costs and the potential impacts of the conflict in the Ukraine.
- 2.13. KCC will inevitably have to absorb some of the impact through construction costs that will exceed the current programmes budget levels.

3. Impact Assessment

- 3.1. Capital projects procured before Page 14 crisis peaked in the summer months were delivered to contractual dates and costs, predominantly due to the KCC contractors

procuring early and having the buying power that some smaller contractors lack. Maintenance projects procured in the months leading to the peak of the crisis (summer months 2Q2021/3Q2021) experienced delays due to lack of materials and or long lead times. Some projects could not be procured due to the limited number of suppliers available to tender for smaller projects.

3.2. Although the mitigation measures implemented so far have been sufficient to allow for the delivery of majority of the capital projects, it is now evident that this is no longer sustainable, due to the level of inflation predicted in the coming year and the unknown inflation resulting from the conflict in the Ukraine.

3.3. The KCC construction programmes / projects that will be impacted are split into education and corporate programmes, major highways projects and highways asset management programmes.

3.4. **Education Programmes**

3.4.1. ***The Basic Need Programme***

This delivers new pupil places by expanding existing maintained schools, free schools, or academies, and by establishing new schools. In the next 6 months there is a need to procure construction contracts that are set to deliver over 326 school places. These schemes, based on forecasted tender price indices, will experience the highest impact of the crisis.

Further procurement will also be required for delivery of a further 2,946 school places by September 2023. The impact will be dependent on when the construction contracts will be procured, and the prevailing market conditions at the time.

3.4.2. ***Annual Planned Enhancement Programme***

There are over 330 KCC maintained schools, made up of nurseries, primary and secondary schools. The schools are maintained under this programme which are allocated an annual fixed base budget.

- Day-to-day emergency - £3 million base budget per annum (2022/23).
- Major Projects – These are planned maintenance works, based on condition surveys. There is a £4.9 million base budget per annum, however, the impact has been assessed on a value of £13.9 million worth of works to be procured in the remaining months 2021/2022 and 2022/2023. The reason for the higher value of project works to be procured is:
 - Robust Condition Survey Programme
 - Deferred projects from previous years
 - Facilities Management referrals – that is replacing end of life equipment
 - Schools deferring maintenance works
 - Resultant works from structural surveys
 - Compliance referrals
- Schools Access Initiative – these works involve adjusting schools for accessibility requirements of children and have a £750k base budget per annum. The impact will be assessed on known works planned for the remaining months of 2021/2022 and 2022/2023 valued at £800k.

3.4.3. Modernisation Programme

Schools' upgrade/improvements – The majority of projects involves replacing or repairing temporary school accommodation and there is a base budget of £2million. Inflation is being applied on the identified works required in 2022/2023 valued at £1,723 million

3.5 Corporate Programmes

3.5.1 Modernisation of Assets Programme (MOA)

KCC has over 335 corporate buildings which include libraries, adult education centres, youth clubs, children's centres and offices. The MOA programme covers planned and emergency works with the main items of expenditure including repair and replacement works of roofs, building fabric items, doors, and mechanical and electrical items including boilers, lighting and alarm systems. The MOA is allocated on an annual rolling programme budget and in previous years KCC has also authorised / provided additional one-off funding to support delivery of a backlog of maintenance projects under the Maintenance of Assets Plus (MOA +) programme. The impact assessment has been made on the most likely procurement dates of these projects.

3.5.2 Individual Capital Projects

A number of capital projects have been identified that will be impacted by the increase prices on materials.

3.6 Growth, Environment and Transport

3.6.1 The GET capital programme is significant, with a 10-year budgeted spend of £0.9bn and a 2022/23 budget of £193m. GET is the place-based directorate and the vast majority of spend is within the Highways service. Highways Asset Management "HAM" accounts for £79m, with other projects accounting for the balance (£114m).

3.6.2 Highways Asset Management

The annual budget for Asset Management within Highways is set at approximately £70m but there is some re-phasing of spend for 2022/23 and therefore the budget available is c£79m. The HAM budget (funded by DfT grant and KCC borrowing £25m) is not uplifted annually for inflation, whereas all projects include some level of indexation and price risk. Therefore, the purchasing power of the HAM budget, which is some way short of "steady state" requires more than £100m per year and creates a significant asset management backlog of c£700m and rising. Projections for inflation pressures range from 7-10% and a mid-range pressure of £6m has been included in this report, part of which is the annual unfunded inflation element (c3-4% depending on RPIX indices) with the balance being the latest uplifts caused by the COVID-19 pandemic and the indirect effects of the Russian invasion of Ukraine.

Without further funding, the only way that these inflation pressures can be managed is by further reducing the funding made available in terms of the

asset management approach. Spend will still be allocated on a risk-based approach, but the backlog will inevitably increase in a steeper incline and there is likely to be further pressures on the Urgent and Safety Critical capital budget, including asset failure as well as more reactive revenue works.

3.6.3 Highways Capital Programme

The majority of projects within the Highways Capital Programme are externally funded with monies already awarded or allocated towards delivery. The current programme is based upon earlier cost estimates that were provided as part of the relevant individual business case submissions. So, whilst some projects are currently in the delivery stage, several are due to award contracts within 2022/23, which will highlight further increases in prices and a likely uplift in the total cost. One recent example has demonstrated that the market has reacted with a 19% increase in costs on one large highway improvement scheme.

Although the majority of concern is around base prices rising, the highways programme is also facing material shortages and pressure on the price of fuel (including the end of red diesel). There is also concern over increased labour costs with limited resource availability, due to larger projects such as LTC and HS2 being progressed and a redirection of external funding to the Midlands and North.

It is currently being explored whether additional calls can be made to those providers of grants, however, it should be noted that where this is not possible, the risk remains that KCC will need to fund any additional pressure (including inflation). This is due to the fact that the majority of grant awards require KCC to become the accountable body for these funds and cover any potential overspend.

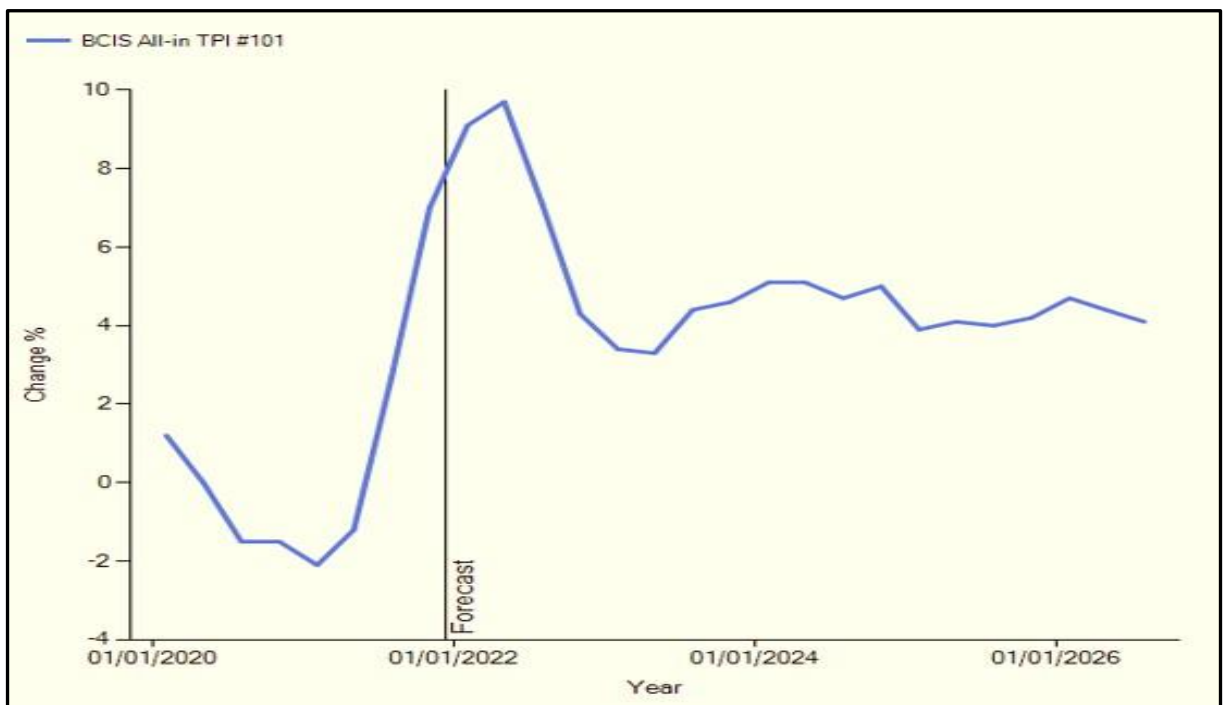
On several projects, the available match funding from S106 contributions will also be challenged as many agreements have indexation clauses which the County Council can call on to cover any potential increase.

4. Contractual Position

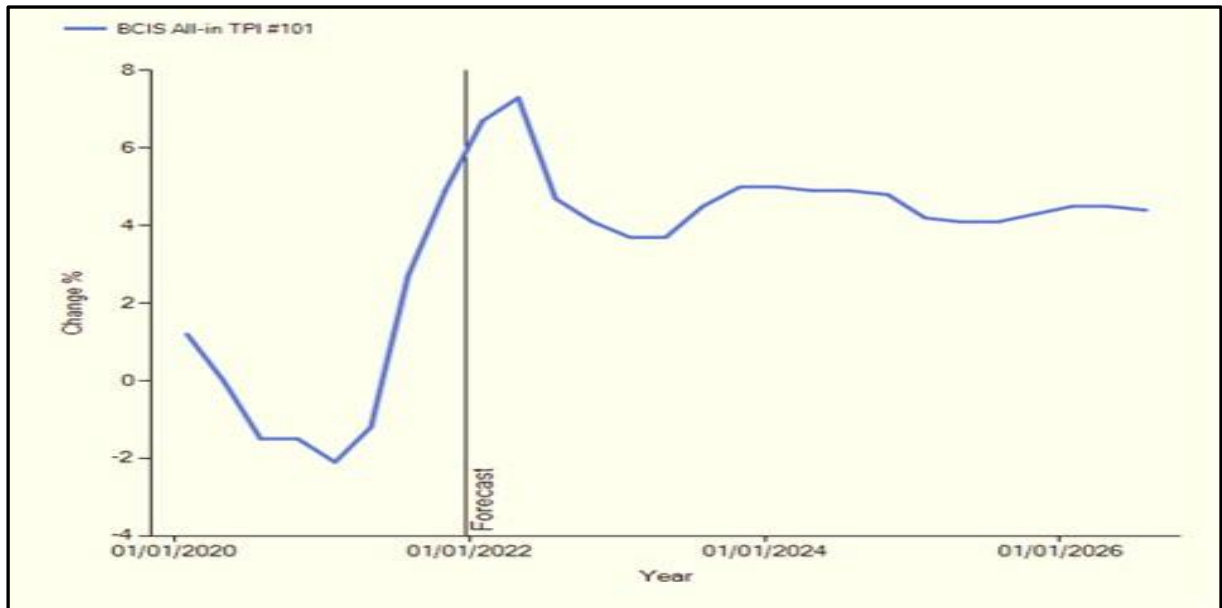
- 4.1. The majority of KCC construction contracts are fixed lump sum contracts. Therefore, once in contract, the risk of material cost increases after the contract date sits with the contractor, unless KCC issue a contract variation. In such instances, the risks of no availability, long lead times and material cost increases in the variation may rest with KCC.
- 4.2. The contractors ordinarily manage this risk by incorporating a risk allowance in their tendered sum. This results in higher tender sums for KCC, but cost certainty on projects. However, since the construction cost inflation started, KCC have been engaging with the main contractor supply chain to manage and control costs using other contractual mechanisms, such as encouraging contractors to place orders early and paying for materials off site using Vesting Certificates or storing the materials on site.
- 4.3. Other contractual mechanisms are available to KCC with varying levels of security and risks. The two key contractual mechanisms available are:

- i) Advanced Payment Bonds (APB) – these can be used to facilitate early procurement to deal with shortage of materials. This solution comes at a premium to KCC (bond security is charged to KCC) and is less suitable to deal with the rise of material costs.
- ii) Fluctuation clauses - KCC retain risk of material costs and adjustments are made based on agreed inflation indices.

4.4. It is expected that contractor tenders will be higher than in previous years as shown above by the forecast from the BCIS TPI indices and the impact assessments. However, the market remains volatile, and the indices are constantly changing to capture market movements. This is reflected in the two graphs below showing the annual predicted changes recorded on 3 December and 17 December 2021. Graph 3 predicted prices would rise and peak at an unprecedented annual rise of 9.7% in 2Q2022. Graph 4 shows the revised position two weeks later to be a predicted annual rise of 7.3%.



Graph 3 - Annual tender price percentage inflation as predicted on 3 December 2021



Graph 4 - Annual tender price percentage inflation as predicted on 17 December 2021

- 4.5. To ensure the level of expected risk included in tenders is not excessive, fluctuation clauses can be used. Using fluctuation clauses can ensure the risk is calculated at the time it is presented. This can be of benefit to both KCC and the main contractor in that KCC do not pay excessive risk allowances included in their tenders and the main contractor has peace of mind that when the prices increase, they will be compensated for it on an open book basis.

5. Financial Implications

- 5.1. The capital allocation for projects / programmes have been set based on historical project cost data. These allocations will no longer be sufficient to cover the expected higher tender prices.
- 5.2. The analysis only includes works that are not in contract (i.e. not included in any contract sums) because works in contract are fixed if KCC do not change the requirements after the contract is let. The analysis has assumed 4Q2021 as the base date of all budgets.
- 5.3. Percentage inflation has been taken to the point when the works will be procured (on the smaller projects or on “phased projects”) and the assumed mid-point of the construction programme (on larger projects).
- 5.4. The current total capital allocation against the programmes identified is insufficient to absorb the additional pressures identified above. Additional funds will need to be allocated to meet the costs. These are summarised in the table below:

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Programme	Forecast	Calculated	Forecast

/Projects	(without inflation)	Inflation Pressure	(with inflation)
Education Projects: <i>Basic Need up to 2023/2024</i>	£125,363,995	£8,740,376	£134,104,371
Education Projects: <i>Annual Planned Enhancement and Modernisation up to 2022/2023</i>	£16,437,955	£334,310	£16,772,265
Corporate Projects: MOA & MOA+ up to 2022/2023	£14,931,921	£674,668	£15,606,589
Corporate Projects: Capital Projects up to 2022/2023	£22,828,435	£1,101,291	£23,929,726
Major Highways Programme*	£114,000,000	£12,000,000	£126,000,000
Highways Asset Management Programme	£79,000,000	£6,000,000	£85,000,000
Total	£372,562,306	£28,850,645	£401,412,951

*calculated on current forecast position before any schemes are removed

- 5.5. The £28.8 million will be used as a contingency figure to cover higher tenders' values and any fluctuation adjustments that may be employed in administering the contracts where it is evidenced that any construction inflation cannot be mitigated.
- 5.6. KCC Infrastructure, Highways and Directorate teams, professional advisors, will continue to liaise with the supply chain to monitor the situation and use all available options to minimise the effects of material inflation.
- 5.7. The market has been volatile in the last twelve months, and it is predicted this will continue for most of the year of 2022 and the expectation is the market will start stabilising nearer the end of 2022 into 2023
- 5.8. As the impact on budgets exceeds £1m and will take the project costs over the allocated budgets, a decision is required to authorise use of funds to meet the effects of material inflation over and above current Record of Decision levels or contract values for contracts which are authorised under delegations.
- 5.9. The current level of inflation is unprecedented and a national issue, which will be impacting on all public sector organisations. Alongside, continuing to lobby government, it is proposed that if it is demonstrated that construction inflation cannot be mitigated, the short-term pressure will be funded from slippage in the current capital programme, which for 2021-22 will be at least £45million. This will require a reprioritisation of the current programme (statutory, health and safety capital spend) removing or delaying lower priority projects that are KCC funded and which have not yet started to deliver a balanced capital programme. It is recognised that over the three year period, there can be no additional prudential borrowing.
- 5.10. There are a number of funding bids which are expected to be announced shortly

which include high needs funding and the DFE school rebuilding programme. These have yet to be finalised and announced, but any success would reduce the current pressure on the capital programme.

6. Legal Implications

- 6.1. In the absence of mitigation action and additional funding in relation to the school projects due to complete for September 2022 and September 2023, KCC will not be able to meet its statutory duties to provide school places in line with the Kent Commissioning Plan or deliver urgent works across the education and corporate estate which could lead to building closure.

7. Equalities Implications

- 7.1. An impact assessment has not been carried out, but it should be noted that failure to implement measures will impact on the delivery and quality of school places and accommodation.

8. Governance

- 8.1. The funding, mitigation activity and delegated authority provided by this decision applies only to capital programme projects approved via the necessary formal governance arrangements (Executive Decision or appropriate delegated authority).

9. Conclusion

- 9.1. The implementation of the rising fuel prices, the ongoing effects of COVID-19 and BREXIT will continue to impact the cost of construction throughout 2022. Current indices show predicted impact on tender prices (as recorded on 17 December 2021), and this reflects that the current capital allocation against the projects / programmes is insufficient. Due to the volatile and unpredicted nature of the crisis the true outcome can only be ascertained nearer the time of procurement and the capital project team have some contractual mechanisms to reduce the impact, but additional funding is required to deliver the schemes included within this report.

10. Recommendation(s)

Recommendation(s):

The Policy and Resources Cabinet Committee is asked to consider and endorse or make recommendations to the Deputy Leader and Cabinet Member for Finance, Corporate and Traded Services on the proposed decision to:

1. Note the £28.8 million estimated impact on capital budget spend in the Medium Term Financial Plan of £339.3 million across the capital programme for 2022-23, were already approved via key decision or covered by appropriate delegated authority to be funded from the options identified in paragraph 5.9 of this report;
2. consider the use of Fluctuation clauses when deemed necessary to control costs to KCC and alleviate adverse effects to the main contractor supplier of the rise in material

costs; and

3. delegate authority to the Director of Infrastructure or for Highway Schemes the Corporate Director of Growth, Environment and Transport in consultation with the Corporate Director of Finance, to take the necessary actions, including but not limited to entering into contracts and other necessary documentation to enable the delivery of the capital programme taking into account construction and inflation where existing Record of Decisions levels are needed to be adjusted.

11. Background documents

- None

12. Contact details

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