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Viability Assessment and Freedom of Information

“Developers must be made to show their sums. Hiding behind commercial confidentiality to keep viability assessments secret is a public betrayal”

Guardian Leader Jan 1st 2015

“We find it particularly hard to accept that the pricing and other assumptions embedded in a viability appraisal are none of the public’s business”

Tribunal Decision on the Greenwich Peninsula. February 5th 2015

My encounter with viability assessment has arisen from on-going ESRC- funded research by the Open University and University of Northampton into new housing development in Northamptonshire and Milton Keynes. Recently, I gave evidence to the recent Third Tier Tribunal hearings into Freedom of Information Appeals into the Heygate development in Southwark, and the Greenwich Peninsula development. My background is as a planner and regeneration officer in local government and an advocate planner for community groups.

This paper covers the following:

- Origins of Viability in the UK Planning system
- Current policy and practice
- Viability - the concept
- Unpicking the viability equation
- Variation due to scheme type
- The viability industry
- EIR (2004) framework
- Arguments against open book
- Arguments for open book

- Recent decisions
- Viability – where do we go from here?
- Implications and Conclusions

Note: The focus of the paper is on viability in relation to section 106 planning obligations. It does not look at viability testing of Local Plans or the Community Infrastructure Levy (though many of the same issues apply)

Viability and planning

The purpose of the planning system is to designate, and regulate, through an accountable and legal framework the appropriate (best) use for the development of land and buildings. It has been an important principle, that development rights flow from policy and plans for sites and buildings, and not from the personal circumstances of the landowner, builder, developer or occupier. Thus, planning policy does not change with every alteration in ownership or every adjustment to the economic circumstances affecting an individual site. These principles provide the context for considering the implications of viability assessment.

What does “viability” mean? By one definition it is holistic concept – the health of an organism. But viability in planning is defined more narrowly as the commercial or financial viability of a development project

Where has viability in planning come from? As far as I aware, although investment appraisal has been common place in the development industry for some time, the concept of viability assessment did not surface in planning guidance until recently. The established method was for planning applications to be considered against approved policy and determined, usually with conditions and, for larger sites, with planning agreements under Section 52 and later Section 106 Agreements. Known as “planning obligations” these payments or contributions were for on- and off-site facilities, mitigation, and infrastructure. They were negotiated between the local authority and developer on a case by case basis within a policy framework set out in the Local Plan - without a requirement to assess the financial implications of these planning obligations on individual applications.

Although in 2005 there was a major new statement on Planning Obligations, it is notable that there was no mention of viability assessment. However, in 2006, the concept of viability assessment surfaced. Planning Policy Statement 3 for Housing said:

'Local Planning Authorities will need to undertake an informed assessment of the economic viability of any thresholds and proportions of affordable housing proposed' [DCLG 2006a, Page 29]

Even so at this stage there was no compulsion that viability assessment would be required.

This changed in 2012 with the publication of the National Planning Policy Framework (NPPF) that emphasised for the first time that Local Planning Authorities (LPAs) must give proper consideration to 'viability' concerns.

Current Policy and Practice

The NPPF does not define viability with any precision or set out a methodology to measure it – rather it stipulates how in the drawing up of new Local Plans and making planning, local planning authorities must pay attention to market viability considerations and the manner in which these impact upon the *deliverability* of housing schemes, taking into account the cumulative effects of local planning policies and standards.

"Plans should be deliverable. Therefore, the sites and scale of development should not be subject to such a scale of obligations and policy burdens that their ability to be developed viably is threatened.

To ensure viability, the costs of any requirements likely to be applied to development should, when taking account of the normal costs of the development and mitigation, provide competitive returns to a willing land owner and willing developer to enable the development to be deliverable" (DCLG 2012, para 173).

The Government's policy on addressing 'viability' in practice was subsequently elaborated in a report commissioned from Sir John Harman (Local Housing Delivery Group, 2012), written specifically to apply the NPPF's viability policy to Local Plans with the aim of increasing the delivery of new house-building.

Harman's group addressed the charge made by house builders that local authorities were routinely applying planning and policy criteria that made potential housing development schemes unviable. The Harman Report stated unequivocally that the aim of viability assessments must be to enable the "deliverability" of plans and building projects.

The report's definition of what viability means is condensed as:

'An individual development can be said to be viable if, after taking account of all costs, including central and local government policy and regulatory costs and the cost and availability of development finance, the scheme provides a competitive return to the developer to ensure that development takes place and generates a land value sufficient to persuade the land owner to sell the land for the development proposed. If these conditions are not met, a scheme will not be delivered' (ibid p.14).

Harman makes the important caveat that positive viability assessments do not mean that development will take place, but that it is more likely to take place if land has reached a "Threshold Land Value" – the value at which a landowner is willing to sell.

The Growth and Infrastructure Act 2013 Review of Section 106 Obligations went further allowing a review of already agreed affordable housing obligations on the grounds of viability:

"An application may be made to the local planning authority for a revised affordable housing obligation. This application should contain revised affordable housing proposals, based upon prevailing viability and should be supported by relevant viability evidence" Para 6 Review and Appeal. This measure is to apply until 2016

The developer will need to demonstrate to the local planning authority and to the Planning Inspectorate on Appeal that the affordable housing obligation as currently agreed makes the scheme unviable in current market conditions" Para 11

It provides a Review and Appeal system if local authorities were unwilling to agree lower levels of affordable housing contributions.

The RICS plays an important role in providing a professional context for viability assessment. In *Financial Viability in Planning* (2012) the RICS emphasise the need for viability assessment to ensure landowners and developers secure “competitive returns”. If a proposed scheme does not ensure a competitive return, the RICS argues that either land will not be brought forward for development or the construction project will not commence.

A very recent change is that sites under 10 units (and changes of use applications) are now excluded altogether from planning obligations either on or off site (National Planning Practice Guidance, December 2014, para 12).

In summary, then, compulsory viability assessment has provided a “get out” clause for developers otherwise compelled to provide planning obligations determined by local planning authorities.

There are perhaps three reasons for this important change to the planning system:

- (1) Long standing resistance from developers to paying “planning gain” or section 106 contributions or obligations to the local planning authority for infrastructure or community facilities
- (2) Additional pressure from developers to reduce obligations because of the impact of the recession on the property market
- (3) Government concern about housing delivery, seeking to reduce “burdens” on developers such as planning obligations

Why is this important?

- (a) Government spending on affordable housing has fallen over the last 10 years. Developer contributions to affordable housing through section 106 is now one of the main ways in which it is provided (Delivering Affordable Housing through section 106, JRF, 2006)
- (b) Viability testing has reduced the percentage of affordable housing especially of social rented homes (In the Mix; The Need for a Diverse Supply of New Homes, Shelter, 2014, p.21)
- (c) Viability testing of affordable housing contributions is undermining statutory local plan policies for affordable housing contributions

(Research by Bureau of Investigative Journalism, September 18th, 2013;
see example 35% Campaign in Southwark)

The NPPF and the Review of Planning Obligations have thus brought viability into the centre stage of planning, as a material consideration. Hence, viability assessment and the right of the public, through freedom of information, to participate in this process is now of major public interest.

Viability Assessment – the concept

Development viability is usually estimated using the Residual Land Value (RLV) method. The RLV is the difference between Development Costs and Development Value.

Viability is assessed by judging whether the RLV is sufficient to generate a profit (“competitive return”) for the landowner and developer, given the amount of planning gain required by the local planning authority. This net value is sometimes called the “Threshold Land Value” i.e. the land value at which a landowner would be willing to sell and the developer to make a sufficient profit.

However, as has been pointed out by many commentators there is no agreed methodology, model or standard data base for making such viability assessments. And because there is no agreed methodology, there is, even among professionals, no agreement about the results of viability assessments (McAllister et al, 2013).

- Common models are the Three Dragons/GLA/HCA/ARGUS models
- Some LAs have their own tool kits e.g. Dorset authorities
- Bespoke developer models (for large schemes)

Unpicking the viability equation

Costs

- Construction (building and infrastructure)

- Finance
- Fees
- Developers profit; 20% taken as standard
- Planning Obligations

Development Value

- Lettable space/unit prices (at *current* prices)

At present, all data inputs data are specific to each site and each developers data (fees, profits, construction contracts), and local market conditions (rents and prices) as assessed by the developer. This leads to viability assessments that are specific to a particular site and the profit requirements of individual developers and landowners.

Some have suggested it would fairer, and closer to the purpose of the planning system, if some of the inputs (e.g. fees, construction costs, profit margins) and outputs (land value and profit) were not site specific but rather “benchmarks”.

McAllister and Wyatt suggest;

“Viability assessments should not be based upon the actual developer’s subjective estimates and expectations regarding costs and revenues and the actual developers circumstances regarding land cost, cost of capital, financial structure, operating costs etc. A development viability test for a proposed scheme should be based upon “typical” or “consensus” estimates and expectations regarding the main inputs to the development viability appraisal”.

This allows the calculation to apply not to a specific developer but to a “typical” developer” (Personal communication to 35% Campaign, based upon research by Pat McAllister and Peter Wyatt, 2014)

Many also argue that a Threshold Land Value should be introduced to determine a reasonable price for land, for example, Existing Use Value plus 20%., instead of a land price from the model reflecting the unique profit requirements and market circumstances of a single landowner of developer.

Major Problems with the model:

- Estimating values for the variables in the model is highly subjective
- There are also serious doubts about using “Current prices” and current market conditions especially for major projects
- Most affordable housing is not in fact a cost but makes itself makes a profit especially with so few social rented properties within the definition of affordable housing
- Large schemes have long time-scales over which viability will vary. Development timescales, forecasts and cash flow will vary over time; the longer the timescale the less reliable the estimates of cash flow
- There may be little meaning in an “average” viability figure for a large site such as an urban extension because there will be different levels of viability for different plots
- Viability assessments are complicated by land trading. Thus while the viability assessment reflects the financial calculations of the initial planning applicant they may not reflect the calculations of the final site owner or housebuilder. Often the planning obligations attached to a scheme are very likely to be challenged by a new developer or landowners. Developers and landowners will sell-on sites with planning permission e.g No Win, No Fee is common (i.e where developers get permission for a landowner who sells-on then gives the developer a share of the profit), or developers sell off parts of larger sites with planning permission to other developers who then try to alter the planning obligations covering for the larger site. This means there is an air of unreality about initial viability assessments in these circumstances.
- 20% (developer profit/risk) is a major issue of contention. It is a large number in the equation and has a big impact on RLV, but is it 20% for all schemes and all developers in all places? It is possible to make a reasonable profit on say 12% which generates a high enough land value and more planning gain.
- RICS advise extensive sensitivity analysis of the model because of large variations, but is it actually done, and what does it show?

The Viability Industry

LB Islington statement on cracking down on “artificially pessimistic viability assessments” (Development Viability, London Borough of Islington, 2014)

So great are the financial benefits of reducing planning obligations, there is a “viability Industry” of consultants and agents selling their skills in reducing developer obligations.

- For example, Section 106 Management Ltd. Advertises their services in this way: “Is your scheme stalled by difficult market conditions? Why not use the time otherwise wasted reviewing your section 106 payments and unilateral undertakings and improve the profitability of your scheme”

This contested arena is the context for considering the Freedom of Information issues arising from request for full disclosure of Viability Assessments.

Freedom of Information Issues

Freedom of Information regulations (FOI Act 2000) apply to all public decision making. In the case of large schemes where there is a significant environmental impact, the EIR 2004 12 (5)(e) apply.

The EIR states that “there should be disclosure except where the disclosure would adversely affect or is likely to prejudice the commercial interests of the council or any third party”. (EIR applies only to public bodies not to private developers).

Reliance upon the exception is always subject to the requirement under 12(1) (b) that the public interest in maintaining the exception outweighs the public interest in disclosing the information i.e what is the balance between the public interest in protecting a legitimate economic interest and the public interest in disclosure. It is for the public authority to define this public interest and assess this balance.

This assessment is not just of interest to landowners, developers and local authorities. It is of particular concern for local communities, who rely upon the local authority to act with responsibility and transparency.

The position of the community is strengthened by the terms of the Aarhus Convention 2001 (Convention on Access to Information, Public Participation in Decision Making and Access to Justice in Environmental Matters) which gives weight to access to information to enable the public to participate in decision making.

Arguments against full disclosure/open book

- *From developer/landowner point of view;*
- They argue that full disclosure would constitute a threat to “legitimate economic interests” and cause commercial harm
- They say that the local authority has seen the full VA under FOI or EIR
- Developer placed at a commercial disadvantage if there is disclosure e.g. Competitors could calculate unit prices and profits; and would know how to be more competitive on price.
- A concern of developers appears to be disclosure of unit pricing figure which has been called the “cornerstone of the viability process”
- Bespoke models are more sensitive (a company “secret”)

- *From a Local Authority point of view:*
- The LA is democratically elected to make decisions and the planning committee has seen it or an officer summary of the VA
- DV or an independent assessor has checked it
- Viability assessment is too complicated for the general public, disclosure will not “illuminate” the debate
- Disclosure in full will make it more difficult to negotiate/it will undermine LA bargaining position with other developers
- Developers would not be as frank with LAs if they knew there was to be full disclosure
- Council received the viability assessment on the grounds that it would remain confidential i.e. they signed a confidentiality agreement

Arguments for full disclosure:

- Open government principle/public scrutiny/community place in decision making (Aarhus Convention and the NPPF)

- The viability assessment model itself is flawed; it cannot be accepted on face value and must be properly interrogated including the sensitivity analysis
- Input data are highly contested e.g. market data for rents and prices used in VAs is often partial
- Contrary to the arguments of the local authorities and developers, the Appeals and Tribunals that have taken place show that disclosure does illuminate the debate
- Unit prices are not secret information (they often come from third parties such as estate agents)
- Disclosure will not stop other developers coming forward because there is competition for sites and most of the information is known; and other developers will do their own VAs
- If there is not full disclosure, the impression is given that decision process lacks transparency e.g. a change in affordable housing contributions is not trivial – it is a very important alteration (see comments by Judge Warren at Heygate and Greenwich Peninsula Appeals)
- Commercial danger has been exaggerated; and there is a lack of evidence to support this
- Closed book approach encourages manipulation of the data by larger developers and landowners (LB Islington, 2014, para 5.3). If there is nothing to hide (because the data can be obtained by a bit of research) why do some developers make such a fuss about disclosure? The Islington report suggests that there is evidence that some developers hide their own private assessment of viability (and profit estimates) which are for the eyes of investors and funders only while putting forward more pessimistic assessments to the local authority.
- Planning decisions should not depend upon individual company circumstances
- Local authorities are significantly under resourced/uncritical – they need all the outside (community) help they can get
- There is evident evasion e.g. Developers try and by-pass EIR by sending their assessments straight to the independent assessor. See Inside Housing, 2015

How are Information challenges and Planning appeals on viability going?

There is an interesting and evolving response from Planning Inspectors and Tribunals.

- Heygate (2014) some openness achieved, after going back to the Tribunal to challenge lack of disclosure
- Greenwich Peninsula (2015) full disclosure after Tribunal
- Walthamstowe Greyhound Stadium – full disclosure
- Stoke Newington JR failed
- Earls Court; DV assessment released in full
- Winchester JR in progress

Where next for Viability Assessment: what the options?

- (a) Change the process. At present a Freedom of Information request if any is made after planning consent has been given and variations are sought, because of common adherence to non disclosure. FOI requests by objectors usually take place after the planning decision has been made – and it does not delay implementation of the decision. If there is a successful FOI challenge, it provides at best a pyrrhic victory for the objectors after the fact. This could be changed by placing the opportunity for the determination of FOI issues within the consultation timescale of the planning application i.e. determination of a planning application cannot be made until after the FOI issues are settled and the community has the chance to examine the full viability assessment.
- (b) Require Open Book for all viability assessments. On the one hand, the DCLG Section 106 Affordable Housing Obligations, Review and Appeal 2013 says; *“Where possible viability assessment should take the form of an open book review of the original viability appraisal”* Para 13. But then it adds; *“At Appeal, if the developer is unwilling to proceed on an open book basis, general evidence of changes in costs and values since permission was granted can be submitted. However, a developer must consider whether his Appeal will provide sufficient evidence for the Planning Inspectorate to make a robust, impartial decision on viability”* para 15

(c) Change the methodology. e.g. Lyons Review of Housing Supply 2014
“There should be a single methodology and guidance clearly identifying the uplift in value arising from the grant of planning permission to enable this to be properly considered as part of the planning process alongside the costs of the necessary infrastructure and affordable housing. Calculation of the appropriate benchmark values for viability assessment should be based upon EUV plus a premium” P.75

“It is essential that site specific negotiations are based upon an open book approach to inform relevant appraisal inputs” P.75

(d) Scrap viability assessment altogether because, as argued above, it has introduced a financial test for development control and land use.

(e) Limit its scope to CIL and Local Plans i.e. the strategic level only

Conclusions

The contested nature of viability assessment itself requires full scrutiny to protect the public interest in planning

Viability assessment has significance for the whole UK planning system because viability assessment challenges the basis upon which planning takes place i.e. it introduces for the first time, financial considerations into decisions over land use which have previously been made on strict “planning” grounds i.e. land use and the environment. In effect, any local plan or Neighbourhood Plan with policies for affordable housing or planning contributions policies (or other infrastructure contributions) can be challenged.

Furthermore, where a mix of housing on a site might have a planning merit in itself, and as a matter of policy, the introduction of viability assessment can remove this planning merit on financial grounds alone.

The questions of transparency goes to the heart of local government – what does the Aarhus Convention mean in the context of local authorities holding back information on viability assessments?

Open book with full disclosure is essential to remove the often secret status of planning gain agreements between developers and local authorities

Open book also protects statutory planning policies agreed in full public consultation, with the expectation that these policies cannot be overturned on financial grounds.

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