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15-2-13

Dear Mr Parker

1.0 Re. Greenwich Peninsula Deed of Variation

Further to the Royal Borough's instructions dated December 2012, to assess the financial viability issues arising from the submission by Quintain plc, who are seeking a Deed of Variation from the S106 agreement entered into in February 2004 regarding the implementation of part of the original Peninsula Masterplan, we are reporting accordingly.

This report refers to the Plots addressed in your report, namely, (para.6.1) M0101, M0103, M0104, M0114, M0115, M0116, M0117, NO601, NO602, NO607 and NO608.

As you know, both this practice and yourself, were closely involved with the original agreement, between 2002 and 2004, and therefore, it is perhaps appropriate that we are again involved in reviewing the very different circumstances that now prevail, with particular reference to the financial appraisal prepared by Quintain and their advisors, most notably BNP Paribas in its revised form – Version2 – dated January 2013.

2.0 Development Appraisals

While you are familiar with the Appraisal methodology, a brief resume can be helpful. Development Appraisal models are in essence simple and can be summarised via the following equation;

Completed Development Value

Minus

Total Construction Costs

Minus

Developers Profit

=

Residual Land Value

Residual Value – what the landowner receives – will normally be the critical variable. If a proposal generates sufficient positive land value, crucial in normal cases, but in this case, far more complex, it will be implemented. If not, unless there may alternative funding sources to bridge the 'gap', the proposal will not go ahead.

The problems with Development Appraisals all stem from the requirement to identify the key variables – values, costs etc.- with some degree of accuracy in advance of implementation. Even on the basis of the standard convention, namely that current values and costs are adopted (not values and costs on completion), this can be very difficult.

Problems with key variables can be summarised as follows:

- Values attached to Completed Development Value are largely dependent on comparable evidence which requires sufficient new development in the locality of a similar size and type, to provide a realistic value base. This is a particular issue in the current market circumstances.

- Development costs are subject to extensive national and local monitoring and can be reasonably accurately assessed in 'normal' circumstances. Increasingly however, with restrictions on greenfield developments and a greater emphasis on brownfield sites, 'exceptional' costs such as decontamination are becoming more common. Such costs can be very difficult to anticipate before detailed site surveys.

- Development value and costs will also be significantly affected by assumptions about the nature and type of affordable housing provision and other Planning Obligations / CIL and on major projects, assumptions about development phasing and infrastructure triggers.

- While Developer's Profit has to be assumed in any appraisal, its level is closely correlated with risk. The greater the risk, the greater the profit level, in part as a contingency against the unexpected.

- Ultimately, the landowner holds the key and will make a decision on implementing the project or not on the basis of return and the potential for market change and thus alternative developments.

In the Greenwich Peninsula case, all these factors, and more, have arisen, in what is undoubtedly an unique case. We have sought to try and summarise the key factors for clarity.

3.0 Context

In terms of background and thus context, the main points are as follows:

There have been various consents since the Master Agreement in 2004 which have been granted and these are detailed in your records. In the particular circumstances, the original consent and Agreement specified that ;

- There were 10,010 homes in the original Masterplan, of which 38% were affordable housing in the total of 53 parcels; and,
- There was an assumption, presented by the applicants, that delivery was based on approximately 500 units pa being implemented for twenty years, an optimistic view at the time as we reported, and subsequently overtaken by events – see Section 5 below.

In fact, the actual delivery / track record is 229 constructed dwellings since 2004, including 60 affordable units, which retrospectively has clearly been very disappointing.

4.0 What's being sought?

Deed of Variation

- Setting side that the original S106 agreement remains a contract and is thus enforceable, the applicants are now seeking various changes summarised in para 6.2 of your report.

5.0 Why should RBG consider this ?

There are various factors which have impacted on the original appraisal and thus the original Planning Agreement.

Changing Circumstances

5.1 Policy changes

- Since the original Master agreement**,** various Government publications have emphasised the importance of balancing planning policies with financial viability. The most recent, the National Planning Policy Framework **(NPPF)** is rightly noted in your report and has been much quoted by the development industry when seeking relief from planning obligations and/or affordable housing as in this case. We would simply comment that in our view, it has never been the Government's intention that financial viability as a material consideration should be absolutely over-riding. Indeed, you note in para. 8.13, the caveat, **"where appropriate".**

5.2 Costs of Infrastructure

- There is no doubt that the costs of site remediation, new infrastructure, the Millenium exhibition etc. have been very considerable , the National Audit Office suggesting in 2008 that EP/HCA had invested £225m. While the parties in that process have changed since 2002, recoupment of Government funding has been a key driver in this case.

5.3 Market circumstances

A further key driver has been the state of the property market since the Master Agreement in 2004. The evidence is all too conclusive . The following tables summarise average Borough wide house prices in Greenwich at key points together with monthly and annual sales volumes.

Average Price	**Date**	**Value**	**Year on year change**
Master Agreement	February 2004	£214,888	+ 6.4%
Market Peak	April 2008	£281,122	+ 8.0%
Market Low	June 2009	£236,227	-15.4%
Current	December 2012	£271,255	+5.4%

Clearly, while the Land Registry data shows some fluctuations from July 2010 to December 2012, overall recent average prices have been fairly consistent but are still well below the peak in Spring 2008. Borough wide sales volumes (all transactions) present a similar picture. Monthly peaks and troughs are shown below.

Monthly Sales Features	
February 2004	Approx. 530 per month
Peak in Mid 2006	Approx. 560 pm
Since January 2008	Consistently lower – approx.200 pm
Low point – January 2009	Under 100 pm
Currently	Between 200 and 300 pm

These features are reflected in the annual sales figures (all transactions) for the Borough shown below.

Annual Borough wide Sales	Number
2004	5099
2005	4599
2006	4709
2007	4895
2008	2264
2009	1940
2010	2227
2011	2378
2012 (Jan-October)	2361

As seen, the sharp decline in sales volume has currently settled at about half that prevalent when the Master Agreement was drawn up and is a significant factor in the stalling of the project.

5.4 The Applicant

The Knight Dragon takeover of the project in 2012 has reignited the scheme with new capital albeit on different terms with the other parties.

5.5 The Significance of Affordable Housing Grant

Utilising allocated Affordable Housing grant before it is lost is a key driver. The changes to the Affordable housing grant regime in February 2011 has significantly altered delivery. Indeed, despite a strong policy position in RBG, few developments have been policy compliant since. The exceptions have broadly been those where 'old' grant monies were allocated and still to be spent. The deadline for the use of 'old' money is a crucial factor in this and other cases.

Overall, this combination of circumstances on the Peninsula has presented RBG with a very different development scenario than that envisaged in 2004.

6.0 Proposed Deed of Variation

On the scale being proposed, (eleven sites), the content of the Deed of Variation is unique in that it seeks to exploit the value gap between the four sites in the north west of the peninsula facing Canary Wharf, where the expectation is unit prices of £670psf without any affordable housing, and the seven sites in the south east including affordable housing, where the sales value anticipated averages £550psf. That variation – 21.8% - in effect provides sufficient cross subsidy, in addition to grant, to deliver 21% affordable housing. This tactic also facilitates the take-up of grant in that the south east sites, subject to consent, can proceed quickly - 'oven ready' in property parlance - and thus meet the grant deadline. In contrast, the north west sites will take longer to deliver.

7.0 Conclusion

The key conclusions that emerge from this proposed Deed of Variation are as follows:

7.1 **Affordable Housing Grant is not lost.** Crucially, approximately £50m of grant is not lost so long as it is used by 2015, albeit that the deadline has been extended by the GLA for 380 affordable units out of the total of 646 until December 2017. Since the south east sites are ready to move forward more quickly than the PQ sites and thus there is a greater likelihood of Affordable grant being used and not lost, there is some reassurance regarding delivery. Nevertheless, even with grant aid, the proposal is still only delivering 21% affordable housing by unit and 25% by habitable rooms. As you know, RBG have been achieving over 20% affordable housing on several sites recently without grant.

7.2 **Loss of affordable is minimised.** A critical question is clearly, does the arrangement which would allow 100% private residential units on four sites deliver the maximum amount of affordable housing overall? This is a difficult estimation because of the number of financial variables on eleven different sites. We have explored this together with the applicants' advisors and we believe that if RBG's normal policy approach to affordable housing was applied to all eleven sites, then the likely loss of affordable units overall would be within the range **150-270** affordable units. The explanation is simply that the loss of market revenue reduces the cross subsidy to the affordable support. (that is 4 + 7 delivers more Affordable Housing overall).

7.3 There is no doubt in our view that a combination of Government agencies in their various guises since 2004 and their desire to achieve at least some recoupment of outlay is the basic reason for low Affordable housing. This was exacerbated by the original terms of Government sale to GPRL including GPRL's contractual arrangement (2004) for drawdown of land related to RPI not land market conditions. The GLA's (2012) acceptance of a reduced land payment has mitigated this to a degree, but in essence, the original land deal has driven this appraisal. That situation was then compounded by an over optimistic view of market outputs. (You will recall that in 2004, the EP/MDL deal suggested a £216m return to EP).

7.4 Overall therefore, we are obliged to recommend this proposed Deed of Variation to you. A combination of circumstances largely beyond the Council have resulted in a very different situation to that envisaged in 2004. Our main concern is setting precedent, not least with the remaining plots within the Masterplan still to come forward.

Yours sincerely,

C.D.Marsh FRICS MRTPI