Elephant Amenity Network 35percent campaign
Comments on Draft Development Viability SPD Nov 2015

We welcome the Draft Development Viability SPD and look forward to its adoption- it is sorely needed. There can be little doubt that developers use viability assessments to evade their responsibility to provide the public benefits planning policy requires, particularly affordable housing. The SPD should go some way to remedying this abuse.

We note that Southwark will be joining Islington and Greenwich borough councils in moving to adopt viability SPDs. The London Assembly planning committee has also recently written to Mayor Boris Johnson urging him to take similar action. We welcome this as the start of moves to solve a London wide problem.

We wish to make the following comments, (figures refer to those of draft SPD, relevant quotes in smaller type, our proposed changes in bold);

3.10 Definition of affordable housing) and the NPPF. The NPPF (2011) identifies three types of affordable housing; social rented housing, affordable rented housing and intermediate housing. These definitions are provided in Table 1.

We note that a change in the NPPF definition of affordable housing is currently under consultation and that the Government intends to include Starter Homes as affordable housing. We do not agree with this proposed change.

Has the Council has made any representations on this point? Further, has the Council given any consideration to how such a change would impact on the VA SPD?

2.3 We follow a sequential approach to securing affordable housing. There is a presumption that affordable housing will be provided on the development site, in line with London Plan Policy 3.12 (Negotiating affordable housing on individual private residential and mixed use schemes).

We strongly support the presumption that affordable housing should be on-site.

2.3 Affordable homes should share access arrangements with market homes where practical and the physical integration of affordable housing among market housing (otherwise known as pepper-potting) is encouraged. However, we recognise that pepper-potting can cause difficulties in managing and servicing properties as this can lead to service charges and maintenance costs which result in the affordable homes failing to meet our definition of affordable.

We strongly support pepper-potting. We strongly object to ‘poor doors’. We do not believe that the entailed costs of pepper-potting should allow poor doors or limit access to amenities for affordable housing tenants.

We therefore propose rewording this paragraph to read ‘Affordable homes should share access arrangements with market homes and the physical

integration of affordable housing among market housing (otherwise known as pepper-potting) is required', deleting the final sentence of paragraph.

2.3 Applicants must justify why affordable housing cannot be physically integrated amongst private housing. Integration is often challenging in the development of flats. In these circumstances we suggest that market and affordable housing could be vertically grouped to keep housing costs affordable. There should be no difference in the appearance of affordable units and private units. Affordable and private tenants should have equal access to communal facilities such as shared gardens and parking areas. Affordable housing should be carefully designed so it can be easily maintained.

Notwithstanding our proposal immediately above, and should it not be adopted, we support vertically grouping.

We propose strengthening this requirement by rewording to say;

'In these circumstances market and affordable housing must be vertically grouped to keep housing costs affordable. There will be no difference in the appearance of affordable units and private units. Affordable and private tenants will have equal access to communal facilities such as shared gardens and parking areas. Affordable housing must be carefully designed so it can be easily maintained.'

2.3 In exceptional circumstances, such as where it is possible to secure a higher level of provision, (London Plan 2015 paragraph 3.74) we may allow affordable housing to be provided off-site. An applicant must clearly demonstrate why it would not be feasible to provide the affordable housing on-site. In these circumstances we will require the provision of affordable housing on another site, or sites. We have a preference for off-site affordable housing in the locality of the proposed development. The floor area of the main development site which is private housing must account for no more than 65% of the combined floor area of the main development site and any off-site provision.

We consider that that this approach is open to abuse, where developers are determined not to have affordable housing, particularly social rent, because they think it will deter private purchasers and therefore require them to lower their free-market prices.

We propose that the Council consider strengthening the conditions for off-site provision in the light of our comment.

2.3 In very exceptional circumstances we may allow a financial contribution in lieu of direct provision of affordable housing. The appropriate value of the financial contribution will be calculated by following two stages of calculation.

Firstly, we will use the viability appraisal for the policy compliant scenario and the proposed scheme to identify the difference in gross development value (GDV) between a policy compliant scheme and the proposed scheme. This identifies the financial benefit to the applicant in not providing on-site affordable housing.

Secondly, we will determine how many habitable rooms could be provided if the level of on-site floorspace required for affordable housing was provided for affordable housing. We will do this by applying the affordable housing floorspace requirement to a policy compliant unit mix using the national minimum space standards. We will then multiply the number of habitable rooms that would have been provided on site by £100,000. The draft Affordable Housing SPD sets out that a £100,000 contribution per habitable room is an appropriate contribution to ensure that any shortfall in affordable housing can be delivered by the council.

Whichever figure is higher will be the in lieu payment we require. This ensures there cannot be a financial advantage to not providing affordable housing on-site or off-site. Applicants are encouraged to deliver off-site affordable housing in preference to an in lieu contribution. However, an in lieu contribution will be required where off-site affordable housing is not provided prior to the occupation of the main development.

We consider that this process is also open to abuse, when developers are determined to reduce their in lieu payments or make them to their own advantage eg by the practice of making payments for the affordable housing requirements of other sites, thereby relieving that development of its own requirement – in effect double counting. Deferred, complicated arrangements combining off-site provision and in lieu payments are particularly vulnerable to this abuse.

We propose that the Council consider strengthening the conditions for in lieu payments in the light of our comment.

We also note that DM1.2 and DM1.3 New Southwark Plan, Preferred Option,Oct 2015 make no reference to the £100,000 tarif in calculating in lieu payments, only differences in GDV, and ask whether the two are consistent.

2.4 We will require a later stage viability review for all schemes which cannot viably provide a policy compliant level of affordable housing. Where the viability of a scheme improves, as demonstrated through a viability review, there will be a requirement to make a financial contribution towards meeting the shortfall in affordable housing provision.

We support this but propose that the amount or minimum proportion of the increased value of the scheme over that anticipated should be specified.

3.2 All viability appraisals must be accompanied by a fully working Argus Developer model that can be tested. We recognise that for larger and more complex schemes, bespoke financial models are often produced in Microsoft Excel. We will accept alternative models provided they explicitly show the calculations and can be fully interrogated and the inputs varied.

We support the requirement that all appraisals should be tested by the same model, in this case Argus, because a consistent approach to viability would seem to require a standard model of measurement. This would also allow a body of decisions to be built up that can inform and refine future appraisals. We note that exceptions may be allowed, no doubt for sound reasons, but in these cases it must be stipulated that

such bespoke models should not be deemed as confidential, and must be fully available to public view and scrutiny.

We therefore proposed adding a sentence to this effect 'When a developer submits a viability assessment devised using a bespoke financial model, that model and all the information used in the model is fully available to public view and scrutiny and that the model and nothing in the model will be held confidential'.

3.2 An executive summary of the viability appraisal which summarises the findings and conclusions of the viability appraisal for the lay reader must be submitted alongside the full viability appraisal in order for the council to validate an application. The executive summary must provide a full supporting narrative to substantiate the inputs and assumptions made in the appraisal. This should be a simplified version of the viability assessment that may aggregate costs and sales information.

We support this requirement, but an executive summary must not be regarded as an alternative to the full viabililty assessment (VA). We are also concerned that aggregating sales information in particular will allow the developer to obscure anticipated sales. We can see no reason why the developer should not supply in full information on this critical assumption.

We therefore propose deleting the final sentence and replacing it with; 'The executive summary is a simplified version of the viability appraisal, but it must not omit or include information that would mislead the lay person. It must include, but no be confined to, the benchmark land value, an explanation of how the benchmark has been calculated, scheme profit, scheme profit on costs, scheme IRR, the gross development value, a schedule of anticipated sales, rental income, and anticipated gross development value'.

We propose that the Council also give consideration to further information requirements to ensure that the executive summary effectively inform the public about all the essential aspects of the full VA.

3.2 All viability appraisals will be reviewed by council officers and may be referred to appointed independent assessors. Applicants will be expected to meet the costs, including and legal costs if appropriate, as specified by the council, associated with reviewing viability appraisals in advance. In the absence of a solicitor's undertaking fees must be paid prior to the validation of an application.

We support this requirement. We acknowledge that referring VAs to specialist independent assessors may have value, but consider that this should the District Valuers Service (DVS), as a public body with, we understand, the widest database of information and knowledge. This would also avoid any conflicts of interest that may arise from using a purely commercial service, which we also believe may have a mind-set less attuned to the public benefit.

We therefore propose that this paragraph is amended to include specific reference to the DVS as the default appraiser.

Notwithstanding this we also believe that building up in-house knowledge and understanding of VAs is vital if the Council is to gain the optimum benefits from private developments for the community. Ensuring this may be outside the remit of the SDP but **we propose that the Council produce a public assessment of the resources needed to fully apply and enforce the SPD.**

4.1 Publication of viability appraisals
Guidance Summary
DVG4.1 Viability appraisals which support pre-application discussions will be treated as confidential. DVG4.2 Viability appraisal executive summaries will be published at the validation stage. A revised viability appraisal executive summary must be submitted prior to determination if the affordable housing content has varied to that set out in the initial viability appraisal executive summary. This will be published prior to determination.
DVG4.3 Viability appraisals will be published in full prior to determination for all non-policy compliant schemes.

We support the full publication of VAs, but much of the value of this SPD will be lost if there is not complete transparency, enabling full public scrutiny and discussion; this requires that the full appraisal be published, along with all the other planning documents, on the Council website at the validation stage, alongside the executive summary, which has the function of aiding understanding.

We do not agree with the arguments that publishing VAs before they are assessed by the Council or its agents might cause public confusion or give rise to expectations that might be disappointed, if the VA is changed during consultation. It is the natural course of planning consultation that application documents are revised in response to public comment – indeed that is surely its purpose – and VAs should not be an exception to this rule. If the Council feels it necessary it could accompany the VA with a standard 'Health Warning' to the effect that is subject to change.

We note that the Royal Borough of Greenwich intends to follow this course; it states in its 'Local Information Requirements List for Planning Applications' (Public Consultation Draft 11 May 2015) that 'This information (*viability assessments*) should be provided to the Royal Borough in its entirety. Applicants should be aware that that the assessment will be made available in the same manner as other documents that form part of the submission' (our italics).

We can also see no reason that the council's assessment of VAs (or those of its agents) should not be published, as they are produced.

We therefore propose that DV4.3 is amended to read: 'Viability appraisals will be published in full at the validation stage and in event no later than 6 weeks before determination. The council's assessments of the VA's (or those of its agents) will also be published in full as they are produced'.

5.1 Guidance Summary

DVG5.3 The BLV is the value below which the current use of the site will be

continued. In appropriate circumstances it may be appropriate to include an uplift within the BLV as an incentive to release the land from its current use for development.

We are concerned that including incentive uplift will inflate land costs. We note that elsewhere in the text it states It is accepted that land (with development potential) does not transact at CUV plus an incentive as landowners will clearly sell for the maximum achievable in the market (pg 30).

We therefore ask that the Council give further consideration to DVG5.3

5.1 The viability of a development will be assessed by: Calculating the market value (MV) of the site assuming, firstly planning consent for a policy compliant scheme and, secondly planning consent for the proposed scheme where this is below minimum policy requirements. The residual method of valuation should be used, but the residual land value (RLV) arising must be cross-referenced against market site comparables.

We do not understand the first sentence of this section. We assume MV is CUV plus incentive, and that two different MVs are being calculated, determining two different RLVs .

On a substantive point, we assume that cross-referencing to market site comparables means to actual market purchase prices of land. We know from the Heygate VA, prepared by Savills, that these figures can be wildly variable (actual land sale £48m, comparables £72m) so question the utility of such comparisons.

We believe that on balance the RLV is the correct measure and that that should be used.

We suggest that this section be reworded and amplified.

5.1

- The BLV will be assessed by reference to the CUV.

Viability will be assessed by comparing the BLV with the MV, assuming planning consent has been granted for the proposed scheme,

The text refers to both CUV and MV as the measure of viability. The relationship between CUV and MV is not necessarily clear without explanation (nor is MV explicit in Figure 2: Valuation of scheme viability).

We suggest rewording this section to make it clearer.

Our understanding of Section 5 is that two schemes will be assessed one which delivers the required amount of affordable housing and one proposed by the developer, which delivers less. In each case a benchmark land value (BLV) will be used to measure viability and if the market value (MV) exceeds this, then the scheme is viable. In both cases planning consent is assumed. The RLV method will be used to determine MV, but it is implied that in each case the MV will be different.

If this is correct then it appears to us that the MV will invariably be lower for a policy compliant scheme, making a policy compliant scheme harder to achieve.

We propose an additional DVG point to the 5.1 Methodological approach, Guidance Summary to say;

'The onus is on the developer to demonstrate why a policy compliant scheme is unachievable, in their assessment of a policy compliant scenario. In the event that a policy compliant scheme cannot be achieved then the proposed non-compliant scheme should only be used to establish a minimum amount of affordable housing, that will then be increased, by reconsidering the scheme, including, but not confined to, realisation costs and risk adjusted profit'.

5.2 Valuing a proposed development scheme

We note a significant difference of approach and emphasis in this Section to that taken by Islington Council in its own Draft Development Viability SPD, July 2015 regarding the usefulness of land sale comparables. The Council says;

The relevance of market site comparables cannot be over-emphasised as they demonstrate the amount that developers are willing to pay for sites having made appropriate assumptions with regard to build costs, finance costs, contingencies, profit levels, marketing and sales costs and revenues. (pg 29)

Islington take a much more sceptical approach, saying that "the 'market value approach' should be treated with caution", quoted here;

6.54. The dangers of reliance on purchase price and market transactions are further identified in the recent RICS research paper. The paper emphasises that *"the historic purchase price should never be used in a development viability appraisal"* and that the direct comparison method used in some appraisals to determine land value input or residual land value benchmarks without taking into account planning obligations to determine the appropriate level of planning obligations *"introduces an element of circularity into the appraisal … which can be used by appellants to their advantage"*. Comparable evidence must be adjusted to take into account current policy requirements otherwise there is a clear risk of encouraging *"developers to overpay for sites and try to recover some or all of this overpayment via reductions in planning obligations"*39.

6.55. For these reasons and in view of its current application, the 'market value approach' should be treated with caution. It is vital that market transactions are fully evidenced and genuinely comparable (as required by PPG), or otherwise adjusted to the circumstances of the application site (including policy requirements and to ensure that transaction values have not been inflated through growth assumptions). The existing use value of the site should always be provided for the application site as well as for comparison sites where possible. The agreed benchmark land values for comparison sites should also be identified where available as these represent land values that have been determined for planning purposes and therefore may provide a more relevant basis for comparison than price paid. Where transactions have been cited that are not adequately comparable or have not been sufficiently

adjusted, limited weight can be given to these and any benchmark land value that is reliant on them.

We note Southwark Council's argument that there is the danger RLV can be significantly under or overestimated and that in consequence

the maximum level of affordable housing is not provided (pg 28)

We therefore suggest that market site cross-checking be augmented and DVG5.11 be amended, by adding after the first sentence the following;

'Market transactions must be fully evidenced and genuinely comparable, or otherwise adjusted to the circumstances of the application site (including policy requirements and to ensure that transaction values have not been inflated through growth assumptions). The agreed benchmark land values for comparison sites should also be identified where available as these represent land values that have been determined for planning purposes and therefore may provide a more relevant basis for comparison than price paid'.

5.3 Guidance Summary
DVG5.11 Benchmark land values (BLV) will be assessed by reference to the current use value (CUV) of the site, excluding hope value, plus an incentive uplift if appropriate (CUV+) i.e. the owner of a vacant derelict site with no revenue and incurring holding costs would not require any incentive to release the site from its current use.

Please see our comment regarding DVG5.3, above

6 Viability appraisal information inputs.

Market comparables - Comparable evidence should be provided to support the assumed value and yield levels.

Please see our comment for DVG5.11 above.

6 Viability appraisal information inputs

Overheads and profit

An explanation is required if the overheads and profit figure is to be stated separately and whether this is an average rate or would apply to all works.

It is not clear whether this is a separate category of profit to 'Developer Profit'.

6 Viability appraisal information inputs

Developer profit

The developer profit should be stated and justified separately. Developer's profit should be included at a rate reflected by the specific risk in the market and having

taken account of other risk mitigation included elsewhere in the cash-flow costs. The appropriate metric to assess profit will depend on the scale of the scheme and its financing. We would expect schemes to demonstrate profit on cost and profit on value. The council will take Internal Rate of Return (IRR) into account if requested by the applicant, provided the development programme and timings of costs and values are fully justified. The cross-referencing exercise to market site comparables will give a good indication of the profit levels assumed in the market for schemes being built out supported by institutional funding.

The question of an acceptable rate of developer's profit is evidently complicated but we believe that developers have taken full advantage of the demand for housing, absence of scrutiny, inertia and local planners lack of knowledge to ratchet up their profit to unacceptable levels and that they have used viability appraisals to do this, with a consequent loss of affordable housing. Further, given this direct relationship between profit and affordable housing we believe that determining profit levels cannot be left solely to developers and requires a rational, transparent approach and full public debate, including full scrutiny of VAs.

It has become accepted amongst developers that 20% profit-on-cost is the 'going rate'. We can find no scientific justification for this figure. Indeed we can see no justification for any 'across the board' figure if the profit level reflects the different risks of each site. Taking account of borrowing costs (which should capture scheme risks) and variations for the size of the scheme and different development periods we believe that a 10-15% IRR range provides both a generous return and sufficient incentive to bring schemes forward and that therefore no non-compliant scheme should be approved with IRR profit above this.

We note the use of various different measures of profit – on costs, on total value, IRR - but have framed our proposed amendment in terms of IRR

We therefore propose amending this section of the table, adding words to the effect that 10-15% IRR range provides both a generous return and sufficient incentive to bring schemes forward and that therefore no non-compliant scheme will be approved with profit above this.

We propose that the Council consider similar caps on profit in terms of profit on costs and profit on value, if more appropriate to a scheme's length and complexity.

7. Viability review mechanisms

We support viability review mechanisms for the reasons given, as vital to ensure that the maximum amount of affordable housing is provided by private developments. However we believe that the mechanism could be strengthened, particularly for long-term phased developments.

We therefore propose that phased non-complaint schemes be subject to two further reviews in addition to the post-implementation review, prior to 25% occupation. These would be i/ a mid-term review prior to the later phases of

development of the early phases ii/ an advanced stage review on the sale of 75% affordable housing. These reviews would take account of any further gain in values, savings in costs etc and be based on actual costs and values.

We note that this is an approach adopted by Islington Borough Council.

15 Feb 2016