

For: Arun District Council Review of Applicant Submitted Viability Position

**Greenhurst & Blastreat,
Fitzalan Road,
Arundel,
BN18 9JS**

**October 2018
(DSP18419F)**

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1. Notes and Limitations

- 1.1.1 The following does not provide formal valuation advice. This review and its findings are intended purely for the purposes of providing Arun District Council (ADC) with an independent check of, and opinion on, the planning applicant's viability information and stated position in this case.
- 1.1.2 This document has been prepared for this specific reason and should not be used for any other purpose without the prior written authority of Dixon Searle Partnership; we accept no responsibility or liability for the consequences of this document being used for a purpose other than for which it was commissioned. To the extent that the document is based on information supplied by others, Dixon Searle Partnership accepts no liability for any loss or damage suffered by the client.
- 1.1.3 We have undertaken this as a desktop exercise as is appropriate for this stage and level of review. For general familiarisation, we have considered the site context from the information supplied by the Council and using available web-based material.
- 1.1.4 The information supplied to DSP to inform and support this review process has been supplied by the prospective / current planning applicant on a confidential basis. In looking at 'Accountability' the July 2018 published revised national Planning Practice Guidance (PPG) on viability says on this; '*Any viability assessment should be prepared on the basis that it will be made publicly available other than in exceptional circumstances.*' Therefore, we suggest that the Council and prospective / current or subsequent planning applicant may wish to consider this aspect together. DSP confirms that we are content for our review information, as contained within this report, to be used as may be considered appropriate by the Council (we assume with the applicant's agreement if necessary).

2. Introduction

- 2.1.1 Dixon Searle Partnership (DSP) has been commissioned by Arun District Council (ADC) to carry out an independent review of the viability information supplied to the Council on behalf of the applicant by Bailey Venning Associates (BVA) and dated March 2018. This is in relation to the proposed redevelopment of Blastreat Limited and Adjoining Greenhurst, Fitzalan Road, Arundel, BN18 9JS.
- 2.1.2 The planning application (ref. AB/36/18/PL) was submitted in full and seeks permission for the demolition of the existing buildings & erection of a block of 46 No. sheltered apartments for the elderly (comprising 22 x one-bedroom apartments & 24 x two-bedroom apartments age restricted to 60 years and over), with associated access electric buggy/cycle stores & refuse bin store & 32 No. parking spaces.
- 2.1.3 The site is stated to extend to c.0.366 hectares and is understood to be located within the Arundel Conservation Area.
- 2.1.4 The Development Plan for the area currently comprises the Arun Local Plan 2011- 2031 which was adopted on 18th July 2018. Policy AH SP2 relates to affordable housing and states:

“For all developments of 11 residential units or more the Council will require a minimum 30% of the total number of units proposed on site to be provided as affordable housing on the same site in the first instance.

Where it can be proven, however, that 30% affordable housing is not viable, then a reduction in the amount of affordable housing on site or off-site provision as part of another development within Arun District may be considered (as agreed with the local planning authority). The provision of affordable housing on a site at less than 30% or on an alternative site or by way of a commuted sum will only normally be allowed in very exceptional circumstances if supported by robust evidence including, where appropriate, viability evidence.

The Council will negotiate the affordable housing tenure mix on development sites from an initial default position of 75% rent and 25% intermediate housing.”

- 2.1.5 In this case the proposed development should provide 13.8 affordable units (assumed to be 13 plus a financial contribution “top up”) which equates to 30% of the total number of units.
- 2.1.6 In presenting their viability position the applicant has supplied to the Council a Viability Statement (VS). The report contains a number of Appendices that provide additional / supporting information in relation to the report text and the assumptions used:
- Threshold Land Value report by Sturt and Company
 - BCIS build costs extract
 - Sheltered housing scheme unit and areas schedule
 - Empty property costs assessment
 - Appraisal model for Sheltered Housing Scheme
- 2.1.7 In addition, we were supplied with a functioning electronic version of the development appraisal carried out utilising Argus Developer software. We have considered the assumptions individually listed within the VS and appraisal and provided our commentary based on those whilst also carrying out sensitivity testing where our opinion differs from that of the applicant’s agent.
- 2.1.8 This report does not consider planning policy or the wider aspects in the background to or associated with the Council’s consideration of this scenario. DSP’s focus is on the submitted residential viability assumptions and therefore the outcomes (scope to generate land value) associated with that aspect of the overall proposals.
- 2.1.9 For background, development viability is a measure that may be defined as *‘the ability of a development project to meet its costs including the cost of planning obligations, while ensuring an appropriate site value for the landowner and a market risk adjusted return to the developer in delivering that project’*¹. Under normal circumstances where a viability appraisal is provided, if the residual land value (RLV) created by a scheme proposal exceeds the existing use value or (in the absence of a clear existing use, potentially an alternative use value) then we usually have a positive viability scenario – i.e. the scheme is much more likely to proceed (on the basis that a reasonable developer profit margin is also reached).

¹ Financial Viability in planning – RICS Guidance note (August 2012)

- 2.1.10 The submitted development appraisal has been run in a way which takes account of the benchmark land value of the site and assesses the level of additional residual potentially available in excess of that after allowing for a fixed developer's profit. Therefore, an approach has been taken that sets out to consider, in the applicant's view, the maximum supportable financial contribution for affordable housing.
- 2.1.11 In this case, the sheltered housing scheme as submitted without affordable housing or Section 106 (S106) contributions is shown to generate a residual land value (RLV) of £280,352 based on a fixed level of developer's profit at 20% GDV. Compared to the assumed benchmark land value (BLV) of £1.595m the scheme is shown to result in a deficit of -£1,314,648.
- 2.1.12 The VS concludes therefore that *"any affordable housing contribution would depress the residual value of the sheltered housing scheme too far below that of the benchmark land value. In such an eventuality sheltered housing would not come forward for development."*
- 2.1.13 This review does not seek to pre-determine any Council positions, but merely sets out our opinion on the submitted viability assumptions and outcomes in order to inform the Council's discussions with the applicant and its decision making; it deals only with viability matters, in accordance with our instructions.
- 2.1.14 Arun District Council requires our opinion as to whether the viability figures and position put forward by the applicant are reasonable. We have therefore considered the information submitted. Following our review of the key assumptions areas, this report provides our views.
- 2.1.15 We have based our review on the submitted Viability Appraisal and the premise that the viability of the scheme should be considered based on the assumption of current costs and values. We then discuss any variation in terms of any deficit (or surplus) created from that base position by altering appraisal assumptions (where there is disagreement if any) utilising the applicant's appraisal as a base.

- 2.1.16 This assessment has been carried out by Dan Hay overseen by Richard Dixon and Rob Searle of DSP, who have many years combined experience in the development industry working for Local Authorities, developers, Housing Associations and in consultancy. As consultants we have a considerable track record of assessing the viability of schemes and assessing the scope for Local Authority planning obligation requirements. This expertise includes viability-related work carried out for many Local Authorities nationwide over the last 16 years or so.
- 2.1.17 The purpose of this report is to provide our overview comments with regard to this individual scheme, on behalf of the Council - taking into account the details as presented. It will then be for the Council to consider this information in the context of the wider planning objectives in accordance with its policy positions and strategies.
- 2.1.18 In carrying out this type of review a key theme for us is to identify whether, in our opinion, any key revenue assumptions have been under-assessed (e.g. sales value estimates) or any key cost estimates (e.g. build costs, fees, etc.) over-assessed – since both of these effects can reduce the stated viability outcome.

3. Review of Submitted Viability Assumptions

- 3.1.1 The following commentary reviews the applicant's submitted viability appraisal assumptions as explained within the VS, related viability appraisal and associated appendices.
- 3.1.2 Primarily the review process considers the fact that the collective impact of the various elements of the cost and value assumptions is of greatest importance, rather than necessarily the individual detailed inputs in isolation. We have considered those figures (the appraisal assumptions) provided, as below. In the background to this we have used our working version appraisal to review the impact of trial changes to particular submitted assumptions.
- 3.1.3 This type of audit / check is carried out so that we can give the Council a feel for whether or not the indicated profit positions are approximately as expected – i.e. informed by a reasonable set of assumptions and appraisal approach.
- 3.1.4 Should there be changes to the scheme proposals this would obviously impact on the appraisal outputs.

Benchmark Land Value (BLV – i.e. view on site value)

- 3.1.5 In all appraisals of this type, the base value (value of the site or premises – e.g. in existing use) is one of the key ingredients of scheme viability. A view needs to be taken on this so that it is sufficient to secure the release of the site for the scheme (sale by the landowner) but is not assumed at such a level that restricts the financial capacity of the scheme to deliver suitable profits (for risk reward), cover all development costs (including any abnormals) and provide for planning obligations as a part of creating sustainable development. This can be a difficult balance to reach, both in terms of developers' dealings with landowners, and Councils' assessments of what a scheme has the capacity to bear.

3.1.6 The RICS Guidance ‘Financial Viability in Planning’² states that:

‘A viability appraisal is taken at a point in time, taking account of costs and values at that date. A site may be purchased some time before a viability assessment takes place and circumstances might change.

This is part of the developer’s risk. Land values can go up or down between the date of purchase and a viability assessment taking place; in a rising market developers benefit, in a falling market they may lose out.

A developer may make unreasonable/overoptimistic assumptions regarding the type and density of development or the extent of planning obligations, which means that it has overpaid for the site’.

3.1.7 The revisions to the Viability PPG and the new NPPF (Updated 24.07.18) now very clearly advise that land value should be based on the value of the existing use plus an appropriate level of premium or uplift to incentivise release of the land for development from its existing use. In regards to how land value should be defined for the purpose of viability assessment it states *‘To define land value for any viability assessment, a benchmark land value should be established on the basis of the existing use value (EUV) of the land, plus a premium for the landowner.’*

3.1.8 The guidance defines existing use value as: *‘the first component of calculating benchmark land value. EUV is the value of the land in its existing use together with the right to implement any development for which there are policy compliant extant planning consents, including realistic deemed consents, but without regard to alternative uses. Existing use value is not the price paid and should disregard hope value. Existing use values will vary depending on the type of site and development types. EUV can be established in collaboration between plan makers, developers and landowners by assessing the value of the specific site or type of site using published sources of information such as agricultural or industrial land values, or if appropriate capitalised rental levels at an appropriate yield. Sources of data can include (but are not limited to): land registry records of transactions; real estate licensed software packages; real estate market reports; real estate research; estate agent websites; property auction results; valuation office agency data; public sector estate/property teams’ locally held evidence.’*

² RICS Professional Guidance – Financial Viability in Planning (August 2012)

3.1.9 It states that a Benchmark Land Value should:

- *'be based upon existing use value*
- *allow for a premium to landowners (including equity resulting from those building their own homes)*
- *reflect the implications of abnormal costs; site-specific infrastructure costs; and professional site fees and*
- *be informed by market evidence including current uses, costs and values wherever possible. Where recent market evidence is used to inform assessment of benchmark land value this evidence should be based on developments which are compliant with policies, including for affordable housing. Where this evidence is not available plan makers and applicants should identify and evidence any adjustments to reflect the cost of policy compliance. This is so that historic benchmark land values of non-policy compliant developments are not used to inflate values over time.'*

3.1.10 It further states that: *'Where viability assessment is used to inform decision making under no circumstances will the price paid for land be a relevant justification for failing to accord with relevant policies in the plan. Local authorities can request data on the price paid for land (or the price expected to be paid through an option agreement).'*

3.1.11 In regards to assuming an alternative use value to determine BLV the guidance states *'For the purpose of viability assessment alternative use value (AUV) refers to the value of land for uses other than its current permitted use, and other than other potential development that requires planning consent, technical consent or unrealistic permitted development with different associated values. AUV of the land may be informative in establishing benchmark land value. If applying alternative uses when establishing benchmark land value these should be limited to those uses which have an existing implementable permission for that use. Where there is no existing implementable permission, plan makers can set out in which circumstances alternative uses can be used. This might include if there is evidence that the alternative use would fully comply with development plan policies, if it can be demonstrated that the alternative use could be implemented on the site in question, if it can be demonstrated there is market demand for that use, and if there is an explanation as to why the alternative use has not been pursued. Where AUV is used this should be supported by evidence of the costs and values of the alternative use to justify the land value. Valuation based on AUV includes the premium to the landowner. If evidence of AUV is being considered the premium to the landowner must not be double counted.'*

3.1.12 The above follows the clear direction of travel that we have seen through other recent guidance. For instance, the Mayor of London's Affordable Housing & Viability SPG states the following:

'The process for establishing an appropriate benchmark land value for a viability assessment is key, because this indicates the threshold for determining whether a scheme is viable or not. A development is typically deemed to be viable if the residual land value is equal to or higher than the benchmark land value, as this is the level at which it is considered that the landowner has received a 'competitive return' and will release the land for development.

The NPPF's benchmark for viability appraisal is that it should "take account of the normal cost of development and mitigation, provide competitive returns to a willing land owner and willing developer to enable the development to be deliverable"

The NPPG is clear that "in all cases, land or site value should: reflect policy requirements and planning obligations and, where applicable, any Community Infrastructure Levy charge"

This is a key requirement because if it is assumed that the granting of planning permission will increase the value of the site, but the costs of meeting planning requirements are not factored in, the site value will be over inflated.

It is for this reason that the Mayor does not consider it appropriate within a development appraisal to apply a fixed land value as an input which is based on price paid for land or a purely aspirational sum sought by a landowner. Land transactions reflect the specific circumstances of the developer whereas planning viability appraisals are typically undertaken on a standardised basis. Reliance on land transactions for sites that are not genuinely comparable or that are based on assumptions of low affordable housing delivery, excess densities or predicted value growth, may lead to inflated site values. This undermines the implementation of Development Plan policies and the ability of planning authorities to deliver sustainable development.

The 'Existing Use Value plus' (EUV+) approach to determining the benchmark land value is based on the current use value of a site plus an appropriate site premium. The principle of this approach is that a landowner should receive at least the value of the land in its 'pre-permission' use, which would normally be lost when bringing forward land for development. A premium is added to provide the landowner with an additional incentive to release the site, having regard to site circumstances.

The benefit of this approach is that it clearly identifies the uplift in value arising from the grant of planning permission because it enables comparison with the value of the site without planning permission.

The NPPG confirms that comparing the current use value of a site with the residual land value generated by the proposed development is an appropriate way to determine whether or not a 'competitive return' is achieved for the land owner.

When determining the EUV+ benchmark:

- The existing use value (EUV) is independent of the proposed scheme. The EUV should be fully justified based on the income generating capacity of the existing use with reference to comparable evidence on rents, which exclude any hope value associated with development on the site or alternative uses. This evidence should relate to sites and buildings of a similar condition and quality or otherwise be appropriately adjusted. Where an existing use and its value to a landowner is due to be retained in a development (and not lost as is usually the case), a lower benchmark would be expected.*
- Premiums above EUV should be justified, reflecting the circumstances of the site and landowner. For a site which does not meet the requirements of the landowner or creates ongoing liabilities/ costs, a lower premium would be expected compared with a site occupied by profit-making businesses that require relocation. The premium could be 20% to 30%, but this must reflect site specific circumstances and may be considerably lower.*

- *As set out in NPPG, in all cases land or site value should reflect Development Plan Policies, planning obligations and CIL. When determining a level of premium that would be sufficient to incentivise release of a site for development and ensure that a landowner receives a 'competitive return', this should take into account the overarching aim of delivering sustainable, policy compliant development and that an uplift in land value is dependent on the grant of full planning consent.*
- *If there is an extant permission on the site, this 'alternative use' can be taken into account when determining the benchmark land value. However, there is no requirement for a 'premium' above this figure. It is for the applicant to weigh up the different options and risk profiles of the potential policy compliant schemes for a site and decide which one to pursue.'*

3.1.13 The SPG goes on to state that: *'If an applicant seeks to use an 'alternative use value' (AUV) approach it must fully reflect policy requirements. In addition, the approach should only be used if the alternative use would fully comply with development plan policies and it can be demonstrated that the alternative use could be implemented on the site in question and there is market demand for that use. Where all these conditions are met and the AUV is being used, there is no requirement for an additional 'plus' element. It is for the applicant to weigh up the different options and risk profiles of the potential schemes for a site and decide which one to pursue. Generally, the Mayor will only accept the use of AUV where there is an existing implementable permission for that use'.*

3.1.14 Through recent Appeals we are also beginning to see a shift towards the 'EUV plus' approach; consistent with the Mayor of London's SPG approach and now further consolidated through updated Planning Practice Guidance for Viability and the National Planning Policy Framework (NPPF).

3.1.15 In this case, the VS states *"Sturt and Co, chartered surveyors and registered valuers, have been asked to assess the value of the site with a view to establishing a benchmark land value for viability purposes."* DSP has been provided with this report as an appendix to the VS.

3.1.16 The site consists of a detached house (Greenhurst) and a number of industrial/warehouse buildings currently occupied by Blastreat. The Threshold Land Value Report (TLVR) has considered the Existing Use Value (EUV) of 3no. separate aspects; the value of the existing dwelling (Greenhurst), the value of a potential garden development plot and the value of the Blastreat premises. To all these existing use value assumptions the TLVR has applied a premium to incentivise the sale of the land. This has led to the following assumptions:

- Greenhurst - £630,000 (£4,220/m²)
- Greenhurst Garden Plot - £200,000 (£11,764.706/ha)
- Blastreat Premises - £765,000

3.1.17 The latest NPPF guidance on viability quite clearly states that *“EUV is the value of the land in its existing use together with the right to implement any development for which there are policy compliant extant planning consents, including realistic deemed consents, but without regard to alternative uses.”* As far as we are aware there is no extant consent to split the site of the existing dwelling house into two plots and therefore it is not appropriate to value the site on this basis. The TLVR has valued the site on an alternative use basis which not only is inappropriate given there is no existing implementable planning consent but also should not include any landowner's premium.

3.1.18 In regards to the existing dwelling the TLVR has provided a list of comparable properties and states that when fully refurbished the dwelling would command a market value of £650,000 (£4,355/m²).

3.1.19 In order to assess whether the assumed EUV for the existing dwelling is reasonable we have carried out our own desktop research of property values using property search engines Rightmove, Land Registry, Zoopla and similar sources to review local market indications for properties within a ½ -mile radius of the site.

3.1.20 According to Rightmove 1no. 4-bedroom detached dwelling has sold over the past year within ½ mile radius of the application site. 12 Torton Hill Road sold for £770,000 (£4,124/m²) on 15th November 2017. This property also benefits from a large family garden. When applying this comparative sales value to the existing dwelling we arrive at a value (once refurbished) of circa £615,500.

- 3.1.21 The TLVR states that *“at the time of the inspection the property was boarded up, but it appeared substantially sound and capable of re-occupation if it was refurbished.”* DSP would therefore expect to see the cost of refurbishing the dwelling removed from the valuation.
- 3.1.22 The TLVR has therefore allowed for refurbishment costs of £125,000 which is stated to equate to £78.61/sq. ft. This results in an assumed EUV figure of £525,000 or £490,500 based on our adjusted figures.
- 3.1.23 DSP has had regard to the latest available (1st September 2018) Build Costs Information Service (BCIS) cost data for ‘rehabilitation/conversion’ of one-off detached housing and rebased to an Arun location factor. This is included below for reference:

Results
 > Rebased to Arun (113; sample 12) Edit

£/m2 study

Description: Rate per m2 gross internal floor area for the building Cost including prelims. ?
 Last updated: 01-Sep-2018 02:05

Maximum age of results: Default period ▾

Building function (Maximum age of projects)	£/m² gross internal floor area						Sample
	Mean	Lowest	Lower quartiles	Median	Upper quartiles	Highest	
Rehabilitation/Conversion							
820.1 'One-off' housing detached (3 units or less) (15)	2,756	739	1,295	2,097	3,173	10,603	22

Results
 > Rebased to Arun (113; sample 12) Edit

£/m2 study

Description: Rate per m2 gross internal floor area for the building Cost including prelims. ?
 Last updated: 01-Sep-2018 02:05

Maximum age of results: 5 years ▾ See below for list of results filtered

Building function (Maximum age of projects)	£/m² gross internal floor area						Sample
	Mean	Lowest	Lower quartiles	Median	Upper quartiles	Highest	
Rehabilitation/Conversion							
820.1 'One-off' housing detached (3 units or less) (5)	1,334	823	-	1,137	-	2,239	4

- 3.1.24 As can be seen above, based on the default data set which includes a sample size of 22no. results the median cost equates to £2,097/m². The 5-year data set which provides more up to date cost data but includes a smaller data set of 4no. results indicates a median quartile cost figure of £1,137/m². It is noted that the default data set also appears to include an anomalous result. For the purposes of this exercise we have applied the 5-year data set cost of £1,137/m² (circa £106/sq. ft.).
- 3.1.25 When applying the refurbishment costs based on BCIS, to the existing dwelling this equates to a total cost of c.£169,720 and results in an updated EUV figure of £445,780. To this we then need to apply some form of landowner's premium. The TLVR has assumed a premium of 20%, which although at the upper end of premiums we would expect to see, we are prepared to accept in this instance. When applying this premium, we arrive at a total BLV figure for the existing dwelling house and garden of £534,936. This is the figure we have assumed for the purposes of our sensitivity testing.
- 3.1.26 In regards to the Blastreat premises, the TLVR states that the property has a total GIA of 1,337m² in addition to 245m² of open fronted storage and canopy space. The accommodation schedule is included below:

Building	Description	Sq M	Sq Ft
Main Building	Two storey offices	75.53	813
	Industrial	649.48	6,991
	Canopy	52.81	568
Period Section	Ground floor industrial	256.54	2,761
	First floor storage and staff	171.40	1,845
Separate Building	Industrial	184.17	1,982
	Canopy	99.84	1,075
Stores	Open fronted Store	72.92	785
	Chemical / plant store	19.68	212
Total		1,582.37	17,032

- 3.1.27 In regards to valuing the site, the TLVR states that *"there are few direct comparables in Arundel itself, due to the lack of an industrial sector and therefore I have drawn conclusions from transactions in the wider locality."*

- 3.1.28 The TLVR has assumed that the commercial buildings will be sold on the basis of vacant possession and has applied a rate of £50/sq. ft. (£538/m²) to the main GIA in addition to £15/sq. ft (£161/m²) to the canopies. A cost of £12/sq. ft has then been applied towards works of stripping out and making good to arrive at an EUV figure of £590,000.
- 3.1.29 In order to assess whether the commercial values assumed within the TLVR are reasonable, DSP has carried out our own desktop research of commercial property values using Costar, Estates Gazette Property Link and other sources to review local market indications. Based on this we do not find the commercial valuation assumptions to be unreasonable.
- 3.1.30 In regards to the correct level of premium to apply to this EUV figure, the TLVR states that *“to encourage an owner occupier, that must relocate or terminate their business to sell a higher premium is required.”* Based on this the TLVR has applied a 30% premium to arrive at a total BLV figure for the commercial premises of £765,000.
- 3.1.31 This level of premium is considered high in our view, considering that the site is being developed for an alternative use it would not appear unreasonable to assume that the site did not meet the requirements of the landowner. The NPPF doesn't provide any clear indication in regards to the percentage uplift which should be applied as a premium, however, the Mayor of London's SPG approach states in regards to premiums that *“For a site which does not meet the requirements of the landowner or creates ongoing liabilities/costs, a lower premium would be expected compared with a site occupied by profit-making businesses that require relocation.”*
- 3.1.32 The TLVR states that Arundel lacks an industrial sector and thus this would provide rationale for the relocation of the Blastreat business. For the purposes of our sensitivity testing we have applied a 20% premium however in our view this could be significantly reduced given the site may well have created ongoing liabilities/costs for the landowner. When applying this premium, we arrive at a total BLV for the commercial premises of £708,000 and therefore a total BLV for the site of £1,242,936 say £1.25m, a reduction of -£345,000 compared to the BLV assumed within the VS.
- 3.1.33 In addition to the BLV assumption, the VS has included acquisition costs based on 5% Stamp Duty Land Tax (SDLT), legal fees of 0.75% and agents' fees of 2%. These costs would appear high in our view, for the purposes of our sensitivity testing we have calculated the SDLT based on our adjusted BLV figure and assumed agents' fees of 1% instead of 2%.

- 3.1.34 Any adjustment which may need to be made to the proposed BLV will clearly impact upon the the level of viability “headroom” available to support additional planning obligations. Therefore, this is suggested for review and likely necessary adjustment. Review of the presented RLV appraisal assumptions follows.

Gross Development Value (GDV)

- 3.1.35 The VS states that it has had reference to the discussion regarding sales values contained within our previous report relating to planning application AB/77/17/PL and *“concur with DSP’s view on sales values however it is necessary to update for the passage of time.”*
- 3.1.36 The VS states that *“Land registry reports that the average value of an apartment in Arun rose from October 2017 to January 2018 (the latest period for which data is available at the time of writing) from £169,114 to £169,912 respectively, an increase of 0.47%. If that price inflation were applied to the average sales value proposed by DSP, it would rise to £4,621.62 per sq m or £430/sq. ft.”*
- 3.1.37 Given the Land Registry data relied upon within the VS is dated January 2018, DSP has revisited this to see if any more recent indicators are available. The Land Registry House Price Index (LRHPI) now provides data up until July 2018 indicating an average value for an apartment of £170,590 which equates to a slightly higher rate of inflation of 0.87%. When applying this to our previous blended sales value assumption of £4,600/m² this equates to an updated sales value assumption of £4,640/m².
- 3.1.38 Given the elapsing of time since our previous review at this site (November 2017) it is appropriate to revisit our preceding sales value assumptions. DSP has therefore carried out our own further desktop research of property values with reference to Land Registry sold prices data (updated using the Land Registry House Price Index (LR HPI)) as well property search sites Rightmove, Zoopla, and similar sources to review local market indications for retirement/sheltered housing apartments.
- 3.1.39 DSP note that 2no. new-build retirement properties are currently on the market at Station Road, Littlehampton BN16 3BH. These properties are noted to have been developed by the applicant for this subject scheme and thus are considered to be good comparables.
- 3.1.40 According to retirementmove.co.uk these 2-bed apartments are being marketed at £495,000 to £565,000 which is considerably higher than the values assumed within the VS which average at around £315,000.

- 3.1.41 In our view therefore, it is appropriate to consider the sensitivity of the submitted appraisal outcome to revised (increased) sales values inputs and see how far these need to be moved to support a surplus outcome (RLV greater than our reset BLV of £1.25m (as per para. 3.1.32 above).
- 3.1.42 For the purposes of our sensitivity testing we have therefore looked at the effects of applying a 10% uplift to the LR HPI updated sales value assumptions (based on re-sales properties) to reflect the higher new build values now identified in the area. This results in updated sales values of £5,104/m² and increases the GDV for the retirement apartments to £15,965,312 an uplift of +£1,485,912 compared to the GDV assumed within the VS.
- 3.1.43 Ground rents have been included at £450 per unit and capitalised at a yield of 5.5%, minus purchasers' costs, resulting in an additional capital receipt of £374,688. Whilst we are happy to see that the ground rent assumption has been increased following our previous review, the yield applied would still appear high in our view. We would usually expect to see ground rent assumptions for retirement properties capitalised at a yield of 5%. When making this adjustment the ground rents result in an additional capital receipt of £412,320 an upward adjustment of +£37,632.
- 3.1.44 It is worth noting that any improvement in the sales value assumptions (compared with a level set at the point of the appraisal) would most likely be reflected in an improvement in scheme viability. Whilst the opposite could also occur (the sales values could fall relative to the assumptions made), that is the developer's (applicant's) risk and such factors need to be kept in mind in making an overall assessment of the applicant's position.

Cost Assumptions – Development Timings & Finance

- 3.1.45 The interest rate is the cost of funds to the scheme developer; it is applied to the net cumulative negative cash balance each month on the scheme as a whole. According to the HCA in its notes to its Development Appraisal Tool: *'The rate applied will depend on the developer, the perceived scheme risk, and the state of the financial markets. There is also a credit interest rate, which is applied should the cumulative month end balance be positive. As a developer normally has other variable borrowings (such as an overdraft), or other investment opportunities, then the value of credit balances in reducing overall finance charges is generally the same as the debit interest charge. A zero rate of credit*

interest is not generally plausible, and will generate significantly erroneous results in a long-term scheme’.

- 3.1.46 The RICS also points out that it is often the case that schemes are modelled at current costs & values i.e. ignoring inflation (as is the case here). In this case RICS Financial Viability in planning paper states in appendix D 4.5 ‘... current values and costs should be used together with a net of inflation finance rate. Such a net of inflation rate would be much lower than a bank rate (which naturally includes inflation expectations)’.
- 3.1.47 The HCEAT appraisal notes beside the finance rate input suggest the use of ‘typically around 1.5% to 3% above the Base Rate’.
- 3.1.48 Finance costs have been included at 7% inclusive of all arrangement fees and monitoring costs and are based on a development programme of 63 months to include 12 months pre-planning, a construction period of 15 months with sales commencing a month post construction and lasting 36 months.
- 3.1.49 The development programme would appear overly conservative in our view. For the purposes of our sensitivity testing we have reduced the pre-construction stage to 6 months and in the absence of any evidence to the contrary have assumed a sales period of 23 months representing 2-unit sales per month which would be more in keeping with other retirement scheme scenario reviews in our experience.
- 3.1.50 The interest rate is also high in our experience, typically, in the recent period we would expect to see finance rates of 6% - 6.5% inclusive of all fees.

Cost Assumptions - Build Costs, Contingencies, Fees and Site-Specific Costs

- 3.1.51 The VS and associated development appraisal have assumed base build costs based on the BCIS data for sheltered housing/supported housing development generally in West Sussex. The 5-year data set has been used to account for current building regulation requirements. At the time of the VS the median BCIS cost was stated to equate to £1,689/m².
- 3.1.52 Whilst DSP agree with this approach we have reviewed the latest BCIS data (updated 1st September 2018) and rebased to an Arun location factor. DSP note that the median quartile figure for 3-storey supported housing (as we understand is proposed here) equates to £1,607/m² - see below.

Results

[Rebased to Arun \(113; sample 12 \)](#) [Edit](#)

£/m2 study

Description: Rate per m2 gross internal floor area for the building Cost including prelims. ?

Last updated: 01-Sep-2018 02:05

Maximum age of results: 5 years ▼

Building function (Maximum age of projects)	£/m² gross internal floor area						Sample
	Mean	Lowest	Lower quartiles	Median	Upper quartiles	Highest	
New build							
843. Supported housing							
Generally (5)	1,785	907	1,380	1,706	2,094	3,498	44
Single storey (5)	1,988	1,589	1,741	2,085	2,124	2,400	5
2-storey (5)	1,810	1,227	1,453	1,710	2,181	2,544	12
3-storey (5)	1,600	907	1,341	1,607	1,873	2,200	16
4-storey or above (5)	1,934	1,103	1,314	1,760	2,359	3,498	11
843.1 Supported housing with shops, restaurants or the like (5)	1,774	1,412	1,580	1,662	1,758	2,813	12

3.1.53 When making this adjustment to the development appraisal, the overall base build cost equates to £7,197,753 a saving of +£367,937 compared to the cost assumed within the VS.

3.1.54 It should also be noted that applying the BCIS build costs to a GIA of 4,479m² would represent a net:gross non saleable floor area adjustment of circa 30.2%. This is a relatively large area of non-saleable floorspace, even in relation to retirement schemes where we appreciate that the ratio tends to be larger than for general market housing. This should, however, be a matter of fact and as such ADC may wish to check the floor areas for completeness.

3.1.55 In addition to the base build costs the VS has allowed for external works at 8% an increase from the 5% allowance previously put to us for this site. This is however still within normal parameters and thus we would not query this further at this stage. Demolition costs of £45,000, professional fees of 10% as well as a contingency of 5% have also been included, all of which are considered to be reasonable assumptions to make.

Cost Assumptions – Section 106 Payments / Community Infrastructure Levy (CIL)

- 3.1.56 The submitted development appraisal does not include any allowance for Section 106 contributions. ADC will need to confirm the S106 requirement as any change in the s106 package of requirements would have an impact on the overall viability of the scheme as viewed through the appraisal - an increase would pull the viability outcome downwards (looking at the effect of this assumption only).
- 3.1.57 In all such reviews, we assume that all requirements that are necessary to make a scheme acceptable in planning terms will have to be included.

Cost Assumptions - Sales & Marketing Fees

- 3.1.58 The development appraisal has included a marketing costs at 4% GDV, agent's sales fees at 2% and legal sale fees at 0.5%. Again, this is one of the assumptions areas that has changed significantly from the previous review (marketing fees were placed at 0.5%). At this testing stage however, we have not altered this assumption within our trial appraisal, in acknowledgement that a sheltered housing scheme may incur higher marketing costs than a private residential scheme and accepting that they were probably pitched too low previously. DSP do however reserve the scope to revisit this assumption.

Cost Assumptions – Empty Property Costs

- 3.1.59 The VS makes allowances for empty property costs totalling £205,786; equivalent to approximately £4,474 per unit.
- 3.1.60 Although we agree that there may be an element of empty property costs here that would often not be so significant in a general market apartments development, this is linked to the overall sales profile. So, whilst this is not normally an assumption seen in viability submissions across a range of scheme types, following a number of reviews of this type of scenario DSP has come to accept its relevance as a more significant cost that is usually accounted for to some degree.
- 3.1.61 At approximately £4,474 per unit, this is however above the typical range for retirement schemes in our experience. For the purposes of our sensitivity testing we have reduced this assumption to £2,000 per unit which would be at the upper end of costs we would expect to see.

Developer's risk reward – profit

- 3.1.62 The development appraisal submitted for review assumes a fixed level of developer's profit at 20% of GDV.
- 3.1.63 Profit requirements vary from site to site and from one developer to another. However, in the recent period we have seen a range of profit scenarios within and outside what we would regard as the normal starting point assumptions of say 15% cost to 20% GDV.
- 3.1.64 It should be noted however that with a policy compliant scheme with on-site affordable housing, the profit level on the affordable housing would be lower – typically 6% to reflect the reduced risk in delivering that form of tenure.
- 3.1.65 Lower profit requirements or expectations are now beginning to be seen quite frequently in our experience. However, there are no “rules” about what can be considered acceptable, and appeal case examples as well as our own significant experience of recent site-specific schemes suggest alternative views.
- 3.1.66 The RICS Guidance³ states that: *“When a developer's return is adopted as the benchmark variable, a scheme should be considered viable, as long as the cost implications of planning obligations are not set at a level at which the developer's return (after allowing for all development costs including site value) falls below that which is acceptable in the market for the risk in undertaking the development scheme. If the cost implications of the obligations erode a developer's return below an acceptable market level for the scheme being assessed, the extent of those obligations will be deemed to make a development unviable as the developer would not proceed on that basis”.*
- 3.1.67 It goes on to state: *“The benchmark return, which is reflected in a developer's profit allowance, should be at a level reflective of the market at the time of the assessment being undertaken. It will include the risks attached to the specific scheme. This will include both property-specific risk, i.e. the direct development risks within the scheme being considered, and also broader market risk issues, such as the strength of the economy and occupational demand, the level of rents and capital values, the level of interest rates and availability of finance. The level of profit required will vary from scheme to scheme, given different risk profiles as well as the stage in the economic cycle. For example, a small scheme constructed over a shorter timeframe may be considered relatively less risky and*

³ RICS - Financial Viability in Planning (GN/94/2012)

therefore attract a lower profit margin, given the exit position is more certain, than a large redevelopment spanning a number of years where the outturn is considerably more uncertain. A development project will only be considered economically viable if a market risk adjusted return is met or exceeds a benchmark risk-adjusted market return”.

3.1.68 The level of profit assumed viable is a matter of debate. In our experience through both numerous site specific cases and strategic viability reviews, typically a profit of 20% for market housing and 6% for affordable housing serves as a *maximum* with numerous examples at appeal indicating lower profit levels as being acceptable, in particular for comparable schemes to that being reviewed here (in particular a recent appeal case in Leeds for a retirement scheme on an urban PDL site) where the Inspector in that case stated *“I find that 18.5% is a reasonable profit margin for the nature of this project, on this brownfield site”*.

3.1.69 Given previous debates with similar applicant interests on this matter, we feel that although a lower level of profit could be assumed based on the continued strength not only of the property market as a whole but also this particular sector whilst still returning a market risk adjusted return, we also need to take into account other factors including agreements reached on other schemes and the potential impact of the wider economic circumstances. However, we also note that the submitted development appraisal and supporting FVA does not produce a profit of 20% on GDV. The actual profit in real terms when deducting the appraisal deficit is c.5.25% on GDV and as such we feel a profit scenario below 20% would be acceptable to the applicant based on the information submitted to us to review. For the purposes of this exercise we have set the level of profit at 17.5% however given the profit position put forward by the applicant, it could be argued that this could be reduced.

4. Summary and Recommendations

4.1.1 The overall approach to assessing the viability of the proposed development appears to be appropriate in our opinion. Although a number of the assumptions appear fair at this stage, there are aspects that we have queried or where a difference of opinion exists.

4.1.2 As part of our audit style approach, we have therefore made a number of trial adjustments to the submitted development appraisal to pressure-test the outcome; explore the extent to which a more positive viability might be possible in our experience. Reviewing the discussion above, these are as follows:

- Benchmark Land Value – suggest downwards adjustment
- Sales Values – suggest upward adjustment
- Ground rents – suggested upwards adjustment
- Finance & Development timings– suggest adjustment
- Build Costs – suggested downwards adjustment in line with latest BCIS figures
- Empty Property Costs – suggested downwards adjustment
- Profit – suggest downward adjustment

4.1.3 These changes increase the Residual Land Value (RLV) to £1,846,881 an improvement to the presented residual value of approximately +£1,566,529. When compared to our adjusted Benchmark Land Value (BLV) figure of £1.25m this results in a surplus of +£596,881 which could be put towards affordable housing

- 4.1.4 Overall therefore, at this stage it is not possible for us to agree with an approach which provides a nil affordable housing contribution. We need to be clear that this is based on current day costs and values assumptions as described within our review, and based on the current scheme and viability information as submitted – we are only able to review the information provided. Any change to the proposals noted here would usually alter the assumptions and the viability view presented.
- 4.1.5 No viability appraisal or review can accurately reflect costs and values until a scheme is built and sold - this is the nature of the viability review process. In this sense the applicant and their agents are in a similar position to DSP in estimating positions – it is not an exact science by any means, and we find that opinions will usually vary. DSP necessarily reserves the scope to revisit assumptions and views at any further discussion, review or Appeal stage.
- 4.1.6 DSP will be happy to advise further as required.

Report Ends

October 2018

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