

For:
Arun District Council

**Re: Pound Place, Roundstone
Lane, Angmering, BN16 4AL**

**Review of Financial Viability
Statement**

November 2018
(DSP 18419G)

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ARUN DISTRICT COUNCIL A/51/18/PL





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1. Background - Notes and Limitations

- 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.
- 1.2 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 (DSP); 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, DSP accepts no liability for any loss or damage suffered by the client.
- 1.3 We have undertaken this as a desk-top exercise, as is appropriate and typical for this type of review. For further general familiarisation we have considered the site context from the information supplied by the Council in relation to its planning functions, and also using available web-based material on the locality and property prices in the vicinity.
- 1.4 DSP is a specialist consultancy working only with Local Authorities on development viability matters. We work on a national basis, though much of our work is in the South East. This work includes previous reviews undertaken and others underway for ADC. Our work is on both strategic / policy level projects and a day to day caseload on site-specific viability reviews, which we conduct rigorously using an "audit" type approach.
- 1.5 The information supplied to DSP to inform and support this review process was noted to have been provided by the planning applicant on a **COMMERCIALLY CONFIDENTIAL BASIS**. The applicant requested that its viability submission and any further supporting or related information will not be disclosed to any third parties under the Freedom of Information Act (Sections 41 and 43(2)) or under the Environmental Information Regulations.
- 1.6 In contrast, we note the Council's web-site stated approach that from May 2016 it intends to publish all viability assessments in cases where the affordable housing policy requirements are not met. This will be for EBC to consider.

- 1.7 We note that consistent with the national policy direction on this, and the approach now by many local authorities, EBC will usually require the open provision of at least some details in order to support the decision-making process. In our experience, increasingly fewer viability submissions are now made in a 'private & confidential' way. 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.'*
- 1.8 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).
- 1.9 The applicant has offered to provide a Non-Technical Summary to the Council if necessary, and has requested that the Council seek their consent before publishing this.
- 1.10 In the circumstances, we request that the Council please notifies DSP and the applicant of any intentions in this respect – at this or any future stage in respect of this case.

2. General – Introduction & context to review/positions

- 2.1 Dixon Searle Partnership (DSP) was commissioned by Arun DC (ADC) to carry out an independent review of the viability information supplied to the Council on behalf of the applicant in this case (Hallmark Care Homes Ltd) by their planning and viability consultants, Turley.
- 2.2 In this case the viability review was undertaken because the applicant has made a submission to ADC whereby they consider that, in order to maintain an adequate level of financial viability, the current development proposal needs to come forward without any affordable housing provision or contribution.
- 2.3 The Financial Viability Statement (FVS) prepared by Turley relates to a planning application – at Pound Place, Roundstone Lane, Angmering, BN16 4AL, for the demolition of the existing property and redevelopment as C2 accommodation

comprising a 71 bed space care home for the elderly. The Council's planning application ref. is A/51/18/PL. We understand that full planning permission is sought.

- 2.4 The existing property is a 5 bedroom house with substantial grounds, surrounded by higher density housing, and adjacent to a significant sized residential development which is under construction.
- 2.5 We note that since the original application was submitted and the FVS was carried out, the applicant has amended the application and reduced the number of bed spaces from 71 to 64. We have not been provided with an updated financial viability statement, or updated costings regarding construction of the scheme, therefore we have assessed the FVS as submitted, on the basis of a 71 bed space care home. It is unlikely that the recent changes would lead to improved viability.
- 2.6 The application is for a Gross Internal Area of 4,337 m², in a two/three storey building (two storey with some rooms in the roof).
- 2.7 The purpose of this report does not extend to considering planning criteria beyond the viability matters that are addressed. Nevertheless, and as in many scenarios, in this instance the planning context links into to the land value and potentially other considerations that may be relevant to reviewing the development viability picture.
- 2.8 The application site is understood to be outside the settlement policy area (built-up area boundary) within which an assumption in favour of sustainable development would be typical. It currently contains residential (Class C3) use, with a 2-storey, 5 bedroom house with indoor swimming pool. As is summarised within the Turley Financial Viability Statement (FVS), a previous outline planning permission was granted in April 2015 for 18 new dwellings to be built on the site whilst retaining the existing property, albeit with its outbuildings removed (including the swimming pool) and the bulk of its associated land given over to the new development.
- 2.9 The FVS has been submitted with the aim of demonstrating the level of planning obligations (s.106) that in the applicant's view can be supported by the proposals from a financial point of view. The submission considers this by looking at the level of surplus that is considered available to support financial contributions after all costs of development (including the developer's profit reward for risk) have been met and the submitted view on land value has been taken into account.

- 2.10 Arun Council's Local Plan 2003 (Policy DEV17 states that in developments of 25 or more homes the Council will seek to secure affordable housing. The Council's Housing Strategy and Enabling Manager has set out the policy requirement to provide 30% affordable housing, either on or off site, equating to 21 units. Our understanding is that ADC's AH policy extends to impact C2 developments (as the proposal is acknowledged to be), and not just C3. This is unusual in our experience. We have not considered it further in the course of this work – in any event it does not affect the review of the submitted viability figures that has been requested of us.
- 2.11 In this case we understand that owing to the nature of the proposed accommodation ADC would instead seek a financial contribution towards meeting AH needs in an alternative way, and amounting to a commuted sum, as set out by the Council's Housing Strategy and Enabling Manager, of £1,680,000 (based on 21 units at £80,000 per unit of payment in lieu of affordable housing).
- 2.12 The FVS submission explains that no planning obligation beyond the affordable housing requirement mentioned above has been sought by the Council. The FVS further states that the development is only able to sustain a planning obligation payment of £12,350.
- 2.13 The Private and Confidential/Turley FVS that we have used as the basis for our review was dated April 2018. This comprised a report that in our view is in a fairly typical format for the purpose; confirming the scheme details, explaining the viability basis and assumptions used and covering the expected areas / headings of:
- Scheme proposals and site overview;
 - Planning and policy context;
 - Approach and methodology;
 - Development value assumptions (including occupancy rates of the care home beds and an adjustment to reflect the time taken to reach the target occupancy rate of 90%)
 - Construction costs
 - Costs of sales (including legals) and marketing;
 - Finance;
 - Development programme
 - Benchmark land value (Turley have discussed both existing use value (EUV) and alternative use value (AUV)
 - Conclusions.

2.14 The submitted Appendices included supporting information as follows:

- 1 Site location plan;
- 2 Cost plan
- 3 BCIS cost report
- 4 Comparative pricing analysis
- 5 Viability appraisal summary report
- 6 Viability appraisal – cashflow print;

2.15 All in all, the information scope reflected that which we would normally expect to receive or, if not, request additional information on.

2.16 ADC sought our views on whether the assumptions used within and the findings of the FVS were reasonable.

2.17 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.

2.18 We can confirm that the appraisal methodology behind the FVS is appropriate in our experience. Turley has used well known and commonly deployed Argus developer software, which is familiar to DSP and one of the industry standards for this purpose, especially once we move away from considering the viability of smaller C3 housing developments. Whilst all such calculations differ from one to another, the tool and approach used in this case again reflects the usual accepted principles and methodology.

2.19 The conclusion of the FVS is that the limit of the supportable s106 package is a commuted sum of £12,350; leaving no further scope for an affordable housing contribution or indeed other s106 contribution. This is based on an assessment which concludes that the residual value of the site (development value less) is only £12,350 above the benchmark land value, even when no provision of affordable housing is allowed for.

2.20 This assessment has been carried out by Nick Molyneux 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 15 years or so.

2.21 The following report section, 3, provides an overview of our findings.

3 Review of Submitted Viability Assumptions & Position

General and supplementary information

- 3.1 The following commentary reviews the applicant's submitted viability appraisal assumptions as explained within the FVS, related viability appraisal and associated appendices.
- 3.2 In our findings and comments provided to the Council, we therefore provided our views on the assumptions used for the submission, and on how those come together. We looked at the development value (based on net income from rents), construction costs, finance costs, legal expenses, fees, and so forth, and Benchmark Land Value.

Benchmark Land Value

- 3.3 We have begun our review with this element of the appraisal, as it is central to Turley's approach to their assessment, and we suggest a different approach should be used.
- 3.4 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 land value 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 Council's assessments of what a scheme has the capacity to bear.
- 3.5 The RICS Guidance 'Financial Viability in Planning'¹ 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.'

¹ RICS Professional Guidance – Financial Viability in Planning (August 2012)

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'.

'Site Value' is defined in the same Guidance as the following: 'Site Value should equate to the market value subject to the following assumption: that the value has regard to development plan policies and all other material planning considerations and disregards that which is contrary to the development plan'. It goes on to say 'It is for the practitioner to consider the relevance or otherwise of the actual purchase price, and whether any weight should be attached to it, having regard to the date of assessment and the Site Value definition as set out in this guidance. Where historic costs (for example remediation works) are stated it is important that these are not reflected in the Site Value (i.e. double counted)'.

- 3.6 However, recent research by the RICS^[3] indicates that the market value approach is not being applied correctly and that *'if market value is based on comparable evidence without proper adjustment to reflect policy compliant planning obligations, this introduces a circularity, which encourages developers to overpay for a site and try to recover some or all of this overpayment via reductions in planning obligations'.*
- 3.7 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] RICS Financial Viability Appraisal in Planning Decisions: Theory and Practice. April 2015

3.8 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.’

3.9 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.’

3.10 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).’

3.11 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.'

- 3.12 It is therefore clear that the only acceptable approaches to defining a benchmark land value for the purposes of a viability assessment, is the EUV+ or exceptionally AUV.
- 3.13 In this case Turley have considered the EUV of the existing property, if it were to be sold as it is – a five bedroom detached house with indoor swimming pool and substantial grounds, and they have concluded that it would be worth £1.125m.
- 3.14 However the alternative use of the site has also been considered, and Turley have concluded that the AUV is £1,478,300, based on the previous outline planning permission for 18 units to be erected in the grounds of the existing property, and retention of the existing property (with reduced building size and amenity).
- 3.15 As stated above, Paragraph 17 of the Government's Planning Practice Guidance (revised July 2018) states that "Where AUV is used this should be supported by evidence of the costs and values of the alternative use to justify the land value".
- 3.16 Turley have not included a costed development appraisal for the approved scheme, and have instead used a benchmark land value for the broad area from the Council's Local Plan Viability Assessment Update 2017. Therefore we do not consider the AUV an appropriate reference for the purposes of this appraisal.

- 3.17 As per the Government's Viability Planning Practice Guidance, we consider the EUV+ approach to be the most appropriate method of assessing the scheme. Therefore we have used the EUV (plus suitable incentive for development) as the Benchmark Land Value in this case.
- 3.18 The FVS notes that the existing house was sold in October 2006 for £935,000. Turley use House Price Inflation for the area and type of property to increase this by 20.5% concludes that a reasonable open market value for the property today would be £1.125m. Turley also compare the sales prices per square foot of nearby properties, which results in a similar estimate. We consider this a reasonable assumption (land registry figures suggest a 20.6% increase since 2006).
- 3.19 We have also looked at comparable properties currently for sale in Angmering, of which there are only three with similar land attached, with the following asking prices:
- Arundel Road, Angmering, 5-bed with ¼ acre plot, £895,000
 - Springfield Close, Littlehampton, 6-bed on a large plot, £1m
 - Ham Manor, Angmering, 5-bed overlooking golf course, £1.25m

This also indicates that Turley's assumption of £1.125m is not unreasonable.

- 3.20 Turley then apply a 20% increase to this figure to reflect the incentive required for the landowner to release the site. We consider this to be a reasonable amount, especially considering the landowner is currently resident on the site.
- 3.21 We are therefore in agreement with Turley's conclusion that the amount required to incentivise release of the land is £1,350,000.

Development Value

- 3.22 The value in the FVS is based on the net income from a 71 bed care home, once all costs are deducted from rent.
- 3.23 This value is arrived at using the standard definition within the industry of 'EBITDARM' (earnings before interest, tax, depreciation and amortization, rent and management). An occupancy rate of 90% is assumed to be achieved after two years of trading. The applicant is projecting a stabilized EBITDARM of 30% as a proportion of revenue, which

is toward the upper end of what is being achieved across the industry, according to the most recent Knight Frank annual review of trading performance in the care home sector.

- 3.24 In order to arrive at a capital value for the bed spaces, Turley have applied a Years Purchase multiplier of 13 (which is a yield of 7.69%) to the above EBITDARM. We agree with Turley that this represents an realistic view of the performance of the asset.
- 3.25 A reduction in value has also been applied to reflect the time it will take to reach the 90% occupancy rate, based on the applicant's assumption that there will be 6 residents occupying the scheme at the point of opening, and a further 3 rooms let per calendar month. This results in a £2,345,506 income shortfall over the first two years of trading.
- 3.26 We are primarily interested in the development activity for the purpose of this appraisal, and not the operating model. However we accept this is one of the ways used to value such premises and the figures do not seem unreasonable. This fits with our wider experience of such schemes – viewed as developments we are aware that they frequently lack viability that shows significant financial headroom.

Development programme

- 3.27 The forecast build programme is a 6-month lead in followed by a 22 month build period, which is in line with what we would expect for a development of this size.

Base construction costs

- 3.28 The applicant has provided a cost plan showing that the basic build cost per square metre is estimated at £1,832. This is in line with BCIS costs for the area and type of housing.
- 3.29 We consider that the assumptions in the FVA are not unreasonable in this respect.
- 3.30 External works have been added at a level that equates to circa 14.3% of the base build costs by our calculation. On review of the site layout proposal plan, we consider this to be a fairly full but not an excessive assumption.

- 3.31 The costs include £47,000 for demolition of the existing house. It is not clear how this cost was arrived at, however it seems a reasonable sum in our view. For completeness, the Council could ask the applicant what this amount was based on.

Professional/technical fees & build cost contingency.

- 3.32 In our view, at 8% build costs these were placed at levels suitable in regard to experience of normal parameters.
- 3.33 Likewise, at 5% of total development costs, contingency has not been placed excessively in our view and experience.

s106 Planning Obligations

- 3.34 Beyond the requirement to provide affordable housing, which the FVS considers to be unviable, there are no planning obligations included in Turley's appraisal.

Finance – interest rate and related assumptions

- 3.35 With an interest rate of 6.5% used and no separately added finance costs (e.g. for arrangement and monitoring or similar fees) this assumption is within normal parameters at the current time – not excessive in our experience.

4. Overview and conclusions

- 3.36 Overall, we have found from our review that a reasonable approach has been taken to the viability assessment. The main point on which we differ from Turley is their use of AUV rather than EUV+ and in our view this should be supported by a proper development appraisal of the scheme granted permission in 2015, or of any other alternative use such as a wholesale redevelopment of the site as residential following demolition of the existing house.
- 3.37 The AUV has not been evidenced. Should a costed appraisal be submitted, this would need further review.
- 3.38 Regarding the value of the care home and the development costs, fees and finance, a reasonably balanced approach has been taken in our view.

- 3.39 The FVS concludes that a policy compliant scheme of 30% affordable housing (or financial equivalent) is not viable. The FVS states that the difference between the Residual Land Value generated by Turley's appraisal (£1,490,000) and the Benchmark Land Value (£1,478,300) is the maximum payable by way of planning contribution. An off site commuted sum of £12,350 is put forward as a suitable payment in lieu of affordable housing.
- 3.40 As mentioned in 3.31 we do not consider the Benchmark Land Value in the FVS to be a suitable figure, and based on the information available currently it is appropriate that the EUV+ method be used, giving a Benchmark Land Value as stated by the applicant of £1,350,000.
- 3.41 We agree that the scheme will not support a policy compliant level of affordable housing. This is in line with our experience deriving from analysis of similar schemes and from CIL viability assessment work, which is that development genuinely falling within Use Class C2 usually has a different viability profile to that associated with C3, owing primarily to the increased development costs overall, and those not being balanced out sufficiently by the values side in many cases.
- 3.42 However, using the EUV+ method we consider that the Council should be able to seek and additional £128,300 in financial contribution - thus a total of £140,650.
- 3.43 As is often the case, the assessment and our review findings are indicative of a scheme where most likely the developer will in the usual way be looking to improve the eventual outturn viability relative to this current stage submission.
- 3.44 As a generally applicable point, should there be changes to the scheme / modifications to proposals that have been assumed to inform the viability submissions and this review, these could change the viability position reached.
- 3.45 If the assessment is revisited on the basis of the recently submitted scheme for 64 bed spaces instead of 71, we would be happy to revisit this appraisal.

Report ends – November 2018

Carried out by: Nick Molyneux, BA (Hons) MCIH

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