Tribal

Thames Gateway South Essex Strategic Housing Group

Housing Viability Support Research Report

January 2010

Improvement East

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1 Introduction

1.1 Background

1.1.1 In 2009, the Thames Gateway South Essex Housing Group commissioned Tribal to deliver a bespoke research and training programme focusing on housing viability assessments. TGSE Housing Group is led by Basildon District Council and works in partnership with Castle Point, Rochford, Southend-on-Sea and Thurrock Councils and partner Registered Social Landlords. The purpose of the research is to address in the short term the economic down turn, its impact on the housing market and options for pursuing alternative investment models.

1.1.2 The project aims to provide planners and housing officers with a better understanding of the viability of affordable housing requirements within the planning process from the early concept stage through to detailed planning consent. This will enable them to be more effective at delivering planning / housing policy when dealing with live schemes, particularly through the art of negotiation.

1.1.3 The project has good alignment with the TGSE Housing Strategy / Action Plan 2008-11 and forms part of the work stream of the TGSE Affordable Housing sub group. It will also complement the proposed Urban Design Training programme also provided by Tribal that will be running in the sub region during the autumn months.

1.1.4 The research stage included a seminar which was held on October 28th 2009 targeting local authority and RSL officers, and will be followed by individual specialist support to local authorities and RSLs.

1.2 Context

1.2.1 Paragraph 29 of Planning Policy Statement 3 (PPS3) states that:

"In Local Development Documents, Local Planning Authorities should…set an overall (ie plan-wide) target for the amount of affordable housing to be provided. The target should reflect the new definition of affordable housing in this PPS. It should also reflect an assessment of the likely economic viability of land for housing within the area, taking account of risks to delivery and drawing on informed assessments of the likely levels of finance available for affordable housing, including public subsidy and the level of developer contribution that can reasonably be secured."

1.2.2 The application of PPS3 was tested during the recent Blyth Valley and Wakefield High Court cases where Local Authorities' affordable housing targets were found to be unsound. These are explored in more detail in Section 4.3.

1.2.3 The approach of each of the Local Authorities in Thames Gateway South Essex therefore needs to be to seek to ensure that the maximum supply of affordable housing is secured to meet as much of the need as possible while avoiding setting targets at a level at which development is deterred, and that this level is underpinned by a robust viability assessment.

1.2.4 And of course, once policy is adopted, there is a need for planners to be able to deliver the policy to secure good quality housing, including a sufficient level of affordable housing to meet needs.

1.3 This Report

1.3.1 It is intended that this report will feed into the review of the Strategic Housing Market Assessment and Strategic Housing Land Availability Assessments. It will also provide useful information regarding supporting evidence to strengthen LDF Core Strategies and Housing Strategies. The report covers the following topics

- Chapter 2: the current Thames Gateway Housing Market
- Chapter 3: Viability assessments
- Chapter 4: Factors affecting housing viability
- Chapter 5: Delivering Affordable Housing / s106 contributions
- Chapter 6: Alternative Investment models
- Chapter 7: Issues arising from Thames Gateway South Essex Housing Seminar

2 Thames Gateway South Essex Housing Market

2.1 Introduction

2.1.1 The three issues which create different patterns of viability in different parts of a local authority area are:

- The existence of markedly different market sub areas with different price levels
- Differences between greenfield and brownfield sites, with respect to both in costs and land owners' expectations of what they expect to receive from the proceeds of development
- Development types and densities, with densities and house types impacting on both build costs and total sales receipts

2.1.2 As well as these differences across a housing market, a number of factors at a site level will affect viability. Some of these are explored below.

2.2 Current market Conditions

2.2.1 In the current market and with high levels of uncertainty in the residential sector the task of setting an affordable housing policy based on evidence that is transparent, practical and deliverable is not an easy one. Because of the sheer lack of activity in the market at the current time, it is very difficult to assess likely sales values, volumes and development periods in the near future (i.e. 6 months to a year).

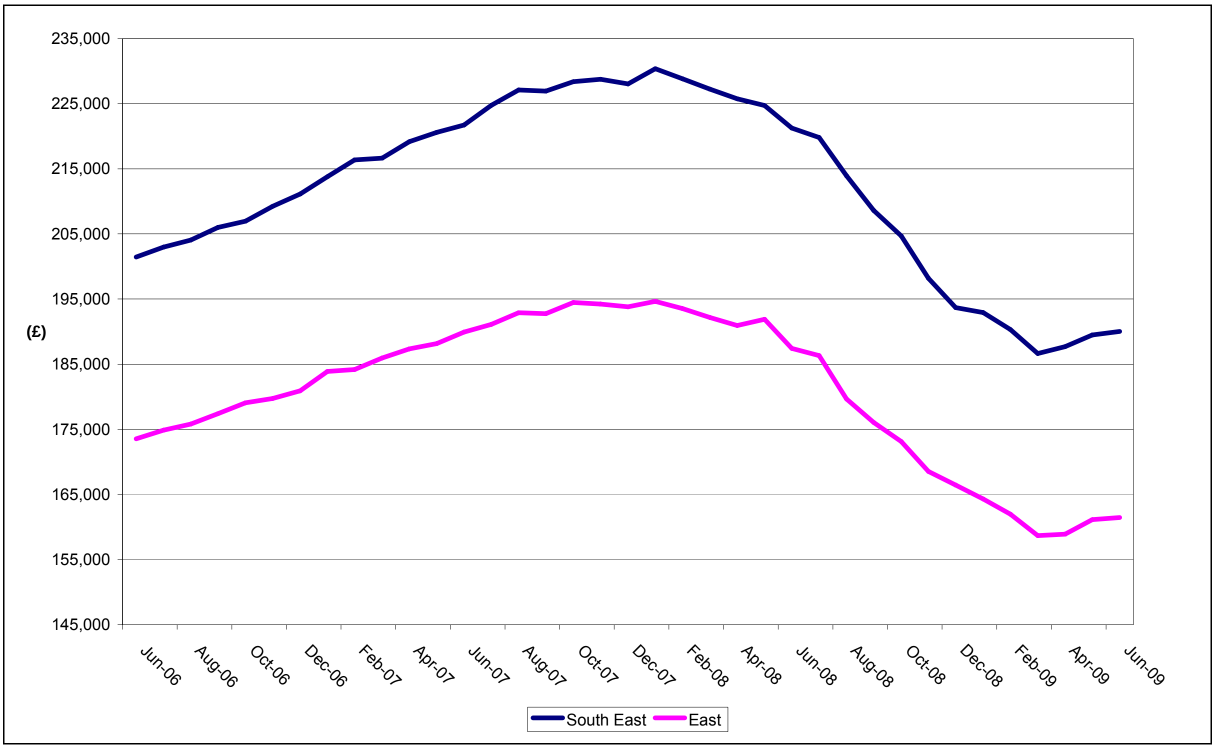
2.2.2 Following a long period of growth in the housing market, house prices reached a peak in the second half of 2007 and the market has now entered a period of falling or static values, particularly in new build.

2.2.3 A key cause of the downturn has been the well documented credit crunch resulting in significant lending restrictions on mortgages and a significant decline in sales.

2.2.4 There remains a range of opinions in the sector, but most commentators report that, despite the Government's £1 billion housing package including raising the stamp duty threshold to £175,000 and initiating a HomeBuy shared equity scheme for a low income first time buyers, this has not been enough to kick start sales and housebuilding while lending is still constrained.

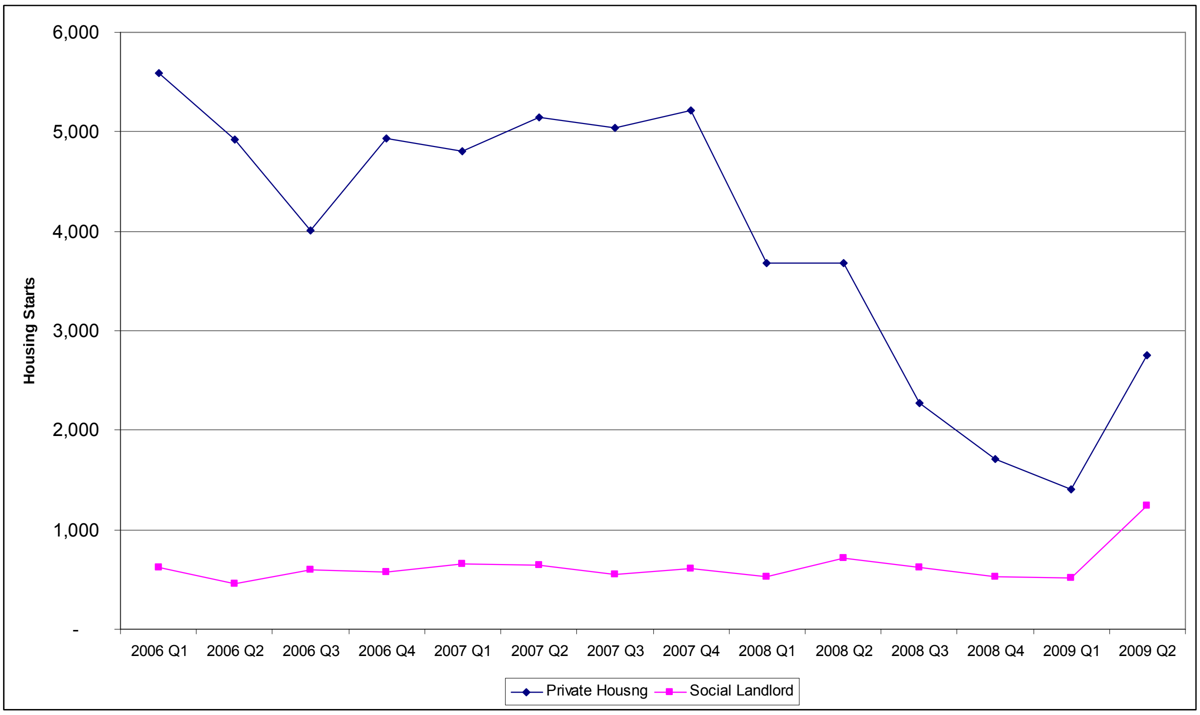
2.2.5 There have been recent early signals that the market may be bottoming out, and there have even been small increases in house prices reported, but it remains a difficult context for Councils to set and test affordable housing policies.

Figure 2-1: Average House Prices 2006-2009



2.2.6 Table 2.1 shows us that sales values in the South East and East of England have dropped by 19% from the peak in December 2007. The drop in sales values value corresponds directly to a reduction in the income generated on development sites. The result is that many housing developments are no longer viable from the perspective of a private sector developer. This reduction in viability is reflected in the number of new housing starts in the East of England.

Figure 2-2: Housing Starts (GOR East) 2006-2009



2.2.7 Figure 2.2 shows a 73% reduction in the number of houses being built by private sector developers in between Q4 2007 and Q1 2009.

2.2.8 Figures 2.1 and 2.2 both show an upturn in the market in Q1 and Q2 of 2009. In terms of assessing viability and the capacity of sites to provide affordable housing there is one key question.

Should viability be assessed against the current market conditions or should assessments be based on future predicted market conditions?

2.2.9 Both approaches have drawbacks. The former method will produce low residual land values which would ultimately result in target affordable housing levels being pessimistically low. The latter forces us to base analyses on housing market forecasts. Given the volatility of housing markets over recent months can this be considered a sound basis to set affordable housing targets?

Normal Market Conditions

2.2.10 The most relevant written guidance available is contained in a recently issued Good Practice Note from the Homes and Communities Agency *Investment and Planning Obligations: Responding to the Downturn.* The note suggests that a robust affordable housing policy for delivering affordable housing in line with PPS12 deliverability criteria and with PPS3 Paragraph 29 financial viability criteria will:

Ensure that any viability study carried out in today's market can not only inform the economics of development today, but also for the whole plan period. The Planning Inspectorate have advised LPAs that it would not be reasonable to base a core strategy on a short term view of the housing market, and that a reasoned assumption on what might be a normal market is needed. Any targets would also need to have been tested and justified, but that provision for flexibility will also be needed to deal with abnormal *market conditions. LPAS are expected to monitor and review policies and adapt them, should abnormal conditions become the norm.*

2.2.11 We have had some discussions with HCA about what form such a flexible policy might take - for example revised SPDs on an annual basis? Their response was that it was not their role to specify to LPAs or their consultants about how this should be done, but that the evidence base should be 'refreshable' or capable of being used in a dynamic market by indexation or other methods.

2.3 Local conditions

2.3.1 Councils are rightly asking themselves how far they need to go to reflect the variations in local conditions that will affect viability. Viability assessment should combine the conflicting interests of local conditions and the need for a policy applicable across the entire study area.

2.3.2 The TGSE SHMA (2008) shows that there is an urban / rural split in regional average house prices, with areas such as Grays, Southend and Basildon showing the lowest house prices. Although house prices have shifted downwards since the SHMA was published, the relative differences between the higher and lower market areas is likely to be the same, if not more marked.

2.3.3 Following a period of falling house prices through 2008 there has been a period of stabilisation in the housing market of TGSE, in line with the wider market in Southern England. Over the last year (April 2008 – May 2009) house prices fell, broadly in line with current trends. The largest decline in average value per unit was in Basildon and Rochford (a decline of just over £20k in each area), followed by Castle Point and Thurrock (£15,000 and £14,000) decreases in each respective area. Prices in Southend fell by £7,500.

2.3.4 There has been a period of stabilisation in prices across the wider region; in TGSE prices have continued to fall in Southend, Rochford and Thurrock, and there has been a slight increase in Castle Point and Basildon. In looking at particular segments of the market, prices in Castle Point and Rochford are consistently higher than in the other three areas for 1-3 bedroom properties, with the highest prices being for 4 bedroom properties in Rochford. Where there have been price increases, these have been for terraced or semi-detached properties, rather than for flats, maisonettes, or detached properties, where prices have continued to fall.

2.3.5 In terms of affordability, a significant proportion of households are priced out of the housing market. For example in Basildon, 37% of households cannot afford to purchase a flat or maisonette as a first time buyer on a mortgage of three times their income. To buy a detached property in Basildon, this rises to 88% of households forced out of this segment of the market.

2.3.6 In terms of activity in the market, the end of 2008 saw a slight rise in both the number of properties being listed on the market, as well as a slight rise in the number of newly registered buyers. However, in 2008 there has been a negative gain the number of newly registered properties, though with slight gains in the number of buyers. This suggests that the rise in prices is mainly a result of a continued increase in demand, against a dwindling number of properties on the market.

2.4 Issues Affecting Affordable Housing in TGSE

Demand issues

2.4.1 The current shortage of affordable housing across TGSE remains a significant issue. The current situation is one which the estimated level of need for affordable housing represents 54% of planned house building. It is extremely unlikely that this demand will be met, as affordable housing planning policy targets are below this, the market has slowed and the number of RSL led developments will not make up the numbers required.

2.4.2 Current affordable housing policies in the Thames Gateway South Essex area set out in Table 1

Table 1: Current Affordable Housing Policy in Thames Gateway South Essex

Local Authority	Current Affordable Housing Policy
Basildon	Require 30% affordable housing on all sites of more than 10 dwellings, except within Basildon and Wickford town centres where only 10% affordable housing should be on the site with the balance of the 30% being either provided off-site or in the form of a commuted sum[1].
Castle Point	Require up to 35% affordable housing on sites over 15 units. In addition, an affordable housing target of 20% on sites of 10 to 14 units, a financial contribution in lieu of on-site provision of 20% on sites of 5 to 9 units and a financial contribution in lieu of on-site provision of 10% on sites of up to 4 units.
Rochford	Require 35% on developments of more than 15 units or on sites greater than 0.5 hectares.
Southend	Require 20% on developments of 10-49 dwellings and 30% on sites of over 50 dwellings.
Thurrock	In order to meet the overall target, the Council will seek to achieve where viable 35% Affordable Housing on all new housing developments capable of accommodating 10 or more dwellings or sites of 0.5 ha or more irrespective of the number of dwellings. Sites below threshold will make a financial contribution equivalent to 20% towards off-site provision.[2]

Source: Thames Gateway South Essex Housing Group

2.4.3 The lack of affordability of market housing, as demonstrated through the ratio of income to house prices and the ability to access finance, is such that there is a decreasing number of first time buyers able to participate in the market, reinforcing the demand for privately rented or social housing.

2.4.4 The current credit squeeze and resulting lack of availability of 100% mortgages and cautious lending approaches from banks and building societies means that those wanting to buy may be unable to. This puts pressures on other tenures over the short to medium term. The severity and length of this squeeze on finance is expected to be longer than

[1] Awaiting ratification through LDF process.

[2] Ibid

was originally thought. Any decrease in prices will be offset in the tightening of the ease of which mortgages are accessed.

2.4.5 There is also likely to be an increase in demand for intermediate tenure housing (consisting of sub-market rent and shared ownership tenures), the potential rate of demand for which has increased at a higher rate then that for social rented or private rented. This is especially due to the difficulties for which younger households and prospective buyers are finding in entering the market.

2.4.6 Overcrowding is also an issue in some areas, for example 16% of households in the social housing market are overcrowded and 14% in the private rented market, compared to 6% across all tenures.

Supply issues

2.4.7 The provision of affordable housing in TGSE starts from a relatively low base, making the provision of affordable housing to meet need especially difficult in current market conditions. 15% of the housing stock in TGSE is social housing, compared to 19% across England as a whole. The provision of affordable housing varies across the sub-region, from 6% of the total stock in Castle Point to 23% in Basildon.

2.4.8 In terms of recent delivery of housing, and in particular social housing, there has been a slight downward trend across the TGSE area in the last ten years. In terms of delivering social housing, there was very limited provision between 2001 and 2004, however delivery did increase over the last 3 years, where social housing as a percentage of the total net completions was 15% in 2005, 6% in 2006 and 8% in 2007. The greatest number of affordable housing units were produced in Thurrock, Southend and Basildon. Castle Point has created relatively low levels of affordable housing in comparison with other areas over the past six years.

2.4.9 In relation to the supply-side, the falls in sales prices of homes is likely to lead to a fall in new housing starts and completions, and a reduction in the number of affordable housing units coming on-stream. This is partly due to the re-phasing of current schemes and the mothballing of intended schemes. This is particularly affecting higher risk developments, in TGSE meaning town centre schemes or those in regeneration areas.

2.4.10 Many developers are also seeking higher profit margins on schemes to allow for market risk, meaning that many marginal schemes are considered unviable, affecting discussions with developers regarding affordable housing requirements on schemes.

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3 Viability Assessments

3.1 Introduction

3.1.1 Viability assessments are based on the concept of Residual Land Value (RLV). The RLV is the price a developer will pay for a piece of land. The developer will derive the RLV from the estimated income he will receive from the sale of the new homes that can be built on the land less the costs of procurement.. This is known as the Gross Development Value (GDV).

3.1.2 The principle of RLV is based on a calculation of ***Development Income less Development Build Cost less Profit & Fees.*** Figure 3.1 shows a simple example of a RLV calculation based on one new home with a sale value of £250 000.. A developer will generally only make the decision to go ahead with a development if he can purchase the land for the RLV figure or less.

Figure 3-1: Residual Land Value Calculation

Development Value	**250,000**
Build Costs	
Infrastructure	20,000
Construction	100,000
Total	120,000
Profit & Fees etc	
Fees	25,000
Interest	10,000
Profit	43,750
Total	78,750
Residual Land Value	51,250

3.2 Appraisal tools and methods

3.2.1 There are a range of appraisal tools available for assessing site viability. All calculate Residual Land Value and all essentially work in the same way.

3.2.2 The basic concept is straightforward. Difficulties arise not from the appraisal tool used itself but in developing values and assumptions of the many variables that drive the modelling, which are discussed in this report.

3.2.3 The successful application of any appraisal tool is dependant upon the development of sound, robust and clearly evidenced assumptions on the cost of development, revenues and benchmark land values. There are several financial modelling tools available to local authorities to assess viability. In the following section we briefly review the main tools and comment on the appropriateness and limitations of each.

The Economic Appraisal Tool

3.2.4 The Economic Appraisal Tool (EAT) was originally developed by the Housing Corporation as a tool to appraise residential and mixed development projects seeking Social Housing Grant from the NAHP alongside developer contributions for affordable housing from planning obligations. The purpose of the tool being to demonstrate whether or not grant was required to support a development which would otherwise not be viable.

3.2.5 The EAT produces a RLV and compares this against the benchmark site value, which represents market value of land derived from its existing use or alternative use.

3.2.6 The latest version (V2 2009) of the tool has been adapted to have the capability to inform the viability modelling to evidence and test LDF planning policy for affordable housing targets.

3.2.7 The key drawbacks with the EAT are.

- Limited modelling inputs and lack of flexibility
- The Cashflow that generates the RLV is hidden from the user

3.2.8 The EAT is being promoted by the HCA for the purposes of viability analysis. With practice and manipulation we have found the model an effective if slightly basic tool. Further to this the EAT is the tool that the HCA will use to analyse bids for grant and to demonstrate added value.

The Three Dragons GLA toolkit

3.2.9 The GLA Toolkit has now been in operation since 2002. It was developed for the GLA by Three Dragons and Nottingham Trent University to test scheme viability in relation to policies in the London Plan. The Toolkit is designed for borough-level policy testing purposes, as well as individual site viability assessments and can be:

- Used as a basis for challenging existing affordable housing targets or for setting new ones;
- Used as a basis for testing site thresholds, potentially with a view to lowering them;
- Used as a basis for setting affordable housing targets for sites coming forward in LDFs;
- Used to assess a specific site to support negotiations with a developer on scheme viability, and its ability to accommodate affordable housing.

3.2.10 The GLA toolkit is similar in principal to the EAT. Both require the user to complete set inputs to calculate a RLV. In our experience the GLA toolkit has a greater range of inputs and allows sites the modelled in greater detail than the EAT. The toolkit is well structured and user friendly.

3.2.11 In addition the GLA toolkit has a number of useful features not available with the EAT.

- Benchmark Values – a series of default assumptions are available for the user if required.
- The discounted cash flow (DCF) model helps users take account of schemes that might run over several years and produces a Net Present Value (NPV)

- Affordability Indicator
- Costs Analysis

3.2.12 As with the EAT the GLA toolkit has fixed inputs and isn't overly flexible. It has also been designed for the Greater London authorities and the benchmark values may not be applicable in other areas. In the latest best practice guidance the HCA refer to the GLA toolkit as being an appropriate tool for assessing viability.

Argus Developer and other Specialised Development Appraisal Software

3.2.13 There are more sophisticated software packages available for appraising developments and producing a residual land value. Argus (formerly known as Circle) are most renowned company and provide a range of software packages for this purpose. Such software packages offer a degree of detail and complexity beyond the two approaches discussed above.

3.2.14 Specialised software packages have to be paid for and a license acquire. The exact cost will depend upon the software package used. More importantly such software packages are not really designed for viability testing to support planning policy. They tend to be more complex and require a greater range of inputs. They are more appropriate for testing individual sites in great detail.

3.3 Large Sites and development phasing

3.3.1 Calculating a residual land value for large sites / regeneration projects can be a complex issue. This is particularly relevant to areas within the Thames Gateway where larger regeneration projects are prevalent. This applies particularly to Thurrock which is characterised by large brownfield sites on ex-industrial land which will need significant physical and social infrastructure investment. The rest of South Essex generally has smaller sites which will require smaller levels of investment in infrastructure.

3.3.2 A particular difficulty with large projects is the timescales involved. Development on large sites is likely to be phased over several years. Both the GLA and EAT toolkits, designed for viability testing and supported by the HCA are not ideal for this purpose.

3.3.3 ***The modelling of larger, phased developments to inform consideration of an approach to the deferment of planning obligations, will require models which can reflect the future dynamics of housing market recovery, changing values and build costs, demonstrate their sensitivities and their consequent potential impacts on the out-turn scheme position.***[3]

3.3.4 Development taking place over longer timescales will be subject to changes in market conditions. Changes in market conditions over the medium term can be forecast with some degree of accuracy. However the longer the development period the less confident we can be in the soundness of the assumptions.

3.3.5 The larger sites therefore require a unique approach to assess their viability. Indeed the HCA acknowledge this issue and promote an approach which recognises that for larger phased developments, viability will change between the first and subsequent phases.

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[3] HCA Good Practice Note Investment and Planning Obligations: Responding to the downturn, July 2009

3.3.6 If the EAT toolkit or the GLA toolkit is being used as a basis for modelling we would suggest an approach based on the following key stages:

- Break sites down into likely sub-phases.

- Infrastructure Costs & Planning Obligations- In reality infrastructure costs and planning obligations would be weighted towards the early phases of development. Consideration needs to be given to the timing of the cost of obligations to assist cash flow and hence improve viability. This needs to be considered on the basis of a transparent approach by all parties to consideration of the development's viability.

- Where a development can be built out in phases, policy requirements for affordable housing from the development could be deferred in early phases and the viability of achieving them in subsequent phases in a recovering market considered before the commencement of each phase.

- Model the phases individually taking the above points into account and allowing for changes in the market and the impact on key assumptions.

- Combine the respective RLVs from the phases to produce an overall site RLV.

3.3.7 In practice it is recommend that viability is re- tested prior to the commencement of each phase. The HCA recommendation is that the first phase of the development is tested only, recognising that re- testing will subsequently be needed.

3.4 Link to Policy

3.4.1 How do we make the policy link effectively with work undertaken on the Strategic Housing Market Assessment, Housing Needs survey and regeneration ambitions? It is essential that these conclusions and recommendations are translated into advice on policy formulation, with particular respect to LDF Core Strategy, and Supplementary Planning Documents.

Viability testing

3.4.2 The recent Blyth Valley and Wakefield cases, explored in this report, demonstrate the importance of ensuring affordable housing policy is underpinned by a robust assessment. This will not only ensure that a Core Strategy is found sound by a Planning Inspector, but more importantly that the policy strikes the right balance between ensuring that the maximum amount of affordable housing is delivered, but does not set the target so high that it will discourage developers from bringing forward sites within the TGSE area.

3.4.3 The process of viability testing provides a sound evidence base to produce recommendations on the viability of

- **the proportion of affordable housing**: the Regional Spatial Strategy for the East of England (May 2008) states that at the regional level, delivery should be monitored against the target for some 35% of housing coming forward through planning permissions to be affordable.

- **mix of affordable housing tenures**: this is a need for an appropriate mix between social rented and intermediate tenures.

- **providing affordable housing in different locations and on different site types:** the viability of development will be different according to location and former use. The

Council may wish to consider using a flexible policy that allows a variation by location or by site type.

- **threshold levels**: paragraph 29 of PPS3 states that the national indicative minimum site size threshold for applying affordable housing requirements is 15 dwellings but Local Planning Authorities can set lower minimum thresholds where viable and practicable.

- **using commuted sums**: In exceptional circumstances the Council may consider the acceptance of provision off-site. This may be in the form of land or completed units elsewhere or through a commuted sum payment in lieu of affordable housing provision on site.

Regional Housing Planning Policy

3.4.4 The Regional Spatial Strategy (May 2008) sets the regional policy for the East of England. Policy H1 states that

Within the overall housing requirement in Policy H1, Development Plan Documents should set appropriate targets for affordable housing taking into account:

- the objectives of the RSS;

- local assessments of affordable housing need, as part of strategic housing market assessments,

- the need where appropriate to set specific, separate targets for social rented and intermediate housing;

- evidence of affordability pressures; and

- the Regional Housing Strategy.

- At the regional level, delivery should be monitored against the target for some 35% of housing coming forward through planning permissions granted after publication of the RSS to be affordable.

Policy considerations

3.4.5 Policy should make clear the cost implications of the policy, including

- a clear statement of financial implications of policy together with other S106 requirements (or CIL)

- Whether the intention is to provide affordable housing without grant and where possible give an indication of , what Housing Associations will be able to pay for units, etc

3.4.6 An important issue to consider is the role of “cascades”. A cascade is a mechanism which enables the form and/or quantum of affordable housing provision to be varied according to the availability of grant funding, thus ensuring that at least a base level of need-related accommodation is provided without compromising overall scheme viability. It can be used to secure delivery in marginal situations and is especially useful for large strategic sites where timescale of development makes grant access hard to predict.

3.4.7 There is also the need to consider off-site provision. Circumstances in which off-site provision might be considered include areas which already have a high proportion of affordable housing, or a situation where a site is only suitable for flats, and it is family housing that is needed. It could also be permitted where affordable housing would be too expensive for occupiers e.g. in a location where the service charges were prohibitively high.

3.4.8 Commuted sums or payment in lieu may be acceptable on the smallest sites where the arithmetic would not work. However there must be a clear basis for payment taking into account cost, grant and land value, and a clear plan for how these payments will be used.

3.4.9 The relationship with wider policy / regeneration and housing objectives should also be considered, including the delivery of housing targets and the delivery of infrastructure through tariffs.

Link with other PPS3 / housing evidence bases

3.4.10 There are a number of housing policy evidence bases required by Planning Policy Statement 3: Housing, which feed into policy development, all of which are linked and should be considered as a whole rather than in isolation.

3.4.11 This evidence base should tell the Council

- whether different requirements in different areas may be driven by variation in viability or need.
- what the scope for grant might be and how grant will create “additionality”. It will give the basis of dialogue with HCA.

3.4.12 The Strategic Housing Market Assessment should inform the housing demand and needs, in terms of overall levels of housing and the mix and tenure. It will also give the level of affordable housing needed and the most appropriate tenure mix (ie social rented or intermediate).

3.4.13 The Strategic Housing Land Availability Assessment will quantify the supply side and give an estimate of the number of houses that could realistically come forward on suitable sites in the Plan period.

3.4.14 The Affordable Housing Viability Assessment tests the level at which affordable housing targets can be set without deterring development.

3.4.15 Together, these three key documents, regularly monitored and updated, satisfy the evidence based policy approach encouraged by PPS3 and will ultimately mean that people have a wider choice of homes, both affordable and market, and will create sustainable, inclusive and mixed communities across the South Essex area.

4 Factors affecting housing viability

4.1 Landowner expectations / benchmark valuation

4.1.1 The expectation of landowners depends on many factors, including the existing use of the land, whether or not it has planning permission, who it is owned by, whether it has already been sold as development land, the local history of land price transactions, expectations of what land prices are likely to be in the future and the extent to which landowners and developers recognise that there are s106 policies which impact on the value of development land.

4.1.2 The land price level at which landowners are willing to release land is clearly a key issue in determining viability. If affordable housing and other demands depress the receipt the land owner receives too much, he/ she is likely to consider that the proceeds per hectare mean that is not worthwhile to give up the land, particularly if there is a likelihood of a change of policy with a new government.

4.1.3 However, it is also important to point out that these policies may be expected to reduce the price of land in the longer term, and so the benchmark should not necessarily be based on recent historic disposal values, but some more sophisticated assessment.

4.1.4 The nature of the existing use tends to have a profound influence on the expectation of the land owner. The general experience is that the expectations tend to be greatest in relation to brownfield sites where it has a value derived from its existing or established use – such owners may be very unwilling to accept the residual value associated with, say, nil grant affordable housing, as it may be less than they paid for it. There may even be other alternative uses which can generate a higher land value.

4.1.5 Owners of undeveloped agricultural land tend to have a different perspective – existing use values for agriculture are so much lower than for development uses that even a development heavily loaded with affordable housing and other S106 requirements will create considerable value for the owners of such land. This is particularly the case for the owners of large development sites. However, historic high prices for green field sites have led landowners (and agents advising them) to expect residential market values considerably in excess of existing use value and it may be some time before there is an acceptance that these are unlikely to return to peak levels and landowners are happy to release land at prices below their original expectations.

4.1.6 Discussions with local housebuilders and developers, RSLs and the District Valuer can give a better view of this. The expectations about acceptable levels of residual value per acre tend to vary in different parts of the country. They are highest in the South East and in London, but are likely to have fallen over the last few months, when both development and agricultural land values have fallen.

4.1.7 Using peak historic values is not appropriate, although landowners may aspire to achieve them. The HCA are aware that maintaining 2007 expectations of land value in 2009 may mean that development is not viable. Therefore selecting appropriate benchmark land values is key to the process.

4.2 Infrastructure requirements and the CIL

4.2.1 There are likely to be several competing claims on the pool of value created by development - often also set out in S 106 agreements. It will be important to understand whether there are, for example, requirements to fund open space, education or highway requirements from the proceeds of development, and whether this is set out as a tariff or rate per house.

4.2.2 The Community Infrastructure Levy (CIL) is a proposed new charge which local authorities in England and Wales will be empowered, but not required, to charge on most types of new development in their area. CIL charges will be based on formulae which relate the size of the charge to the size and character of the development paying it. The proceeds of the levy will be spent on local and sub-regional infrastructure to support the development of the area.[4]

4.2.3 The Levy, which is currently under consultation by Communities and Local Government, is designed to improve predictability and certainty for developers as to what they will be asked to contribute; will increase fairness by broadening the range of developments asked to contribute; will allow the cumulative impact of small developments to be better addressed; and will enable important sub-regional infrastructure to be funded.

4.2.4 Key features of the CIL include:

- Those authorities who prepare development plans should be charging authorities.
- There should be an up to date development plan for an area before CIL is be charged.
- Taking other funding sources into account, the charging authority should identify gaps in funding to arrive at a proposed amount to be raised from CIL, subject to an assessment of local development viability at the plan level.
- CIL should be used to fund the infrastructure needs of development contemplated by the development plan for the area, not to remedy existing deficiencies.
- CIL is envisaged as a charge per building (a “roof tax”) rather than a charge for development more generally.
- affordable housing provision should continue to be provided through the existing system of negotiated planning obligations, not through CIL.
- The charging authority should at the same time prepare a draft charging schedule, which will be a new type of document within the Local Development Framework.
- The charging schedule should allocate the proposed amount to be raised from CIL to each main class of development envisaged by the development plan. Charges will be expressed as a cost per square metre of floor space. Charges will be linked to an index of inflation. In drawing up the charging schedule, the charging authority will need to be careful that CIL should not be set at such a level that it risks the delivery of its development plan, because development is rendered unviable by the charge proposed. There will therefore need to be a feedback loop between the process of developing the charging schedule and the process of infrastructure planning.
- Regulations implementing CIL will come into force on 6 April 2010.

[4] Community Infrastructure Levy Detailed proposals and draft regulations for the introduction of the Community Infrastructure Levy, CLG, 30th July 2009

4.3 Stakeholder buy in

4.3.1 Under Planning Policy Statement 3 (PPS3) the Council will need to show that its policy is viable and deliverable. The assessment is an important part of the LDF and core strategy development process and is subject to challenge from external parties such as developers.

4.3.2 In the recent past there have been a number of cases where external parties have successfully challenged affordable housing targets.

Case Study 1 – Blyth Valley
Persimmon Homes, Barratt Homes and Millhouse Developments v Blyth Valley Borough Council The council proposed a requirement of 30 per cent in its emerging core strategy. It then published a statement purporting to assess whether the core strategy was consistent with PPS3. The public examination at the Court of Appeal heard objections from house builders relating to the target and the threshold. They claimed that the study did not provide a robust and credible evidence base for the 30 per cent affordable housing figure. They also cited the secretary of state's decision on a major allocated site in Blyth, where the same consultants had found that the 30 per cent requirement would be unviable.

Case Study 2 – Wakefield
Persimmon Homes, Barratt Homes and Millhouse Developments v Blyth Valley Borough Council ***Wakefield v Barratt Homes*** In July 2008, Barratt made ‘Blyth Valley’ style representations that there had been no AHVS. The Inspector agreed that the submitted documents were not sound. Two economic viability studies were then prepared used to revise the policies. The subsequent Inspector’s report (in March 2009) found revised policies, clearly based on very detailed viability assessment, to be sound. In June 2009, Barratt sought to overturn the policy on the basis that ‘planning inspector was wrong to recommend that the affordable homes policy be modified and failed to give proper reasoning.’ The legal challenge appears to be as much on procedure as on the policy itself. ***‘In my opinion, the lack of transparency of some of the original data upon which assumptions are based is unfortunate and in breach of the justification test requirements’***[5]

4.3.3 In assessing viability it is essential that all parties are involved in shaping policy, which will help to resolve any issues before an Examination in Public of the LDF. The HCA state

[5] (Inspectors Report to City of Wakefield Metropolitan District Council, March 2009)

that one of the good practice principles that viability assessments must adhere to is 'transparent viability'.

The HCA will strongly encourage stakeholders to employ a transparent approach to considering viability where HCA investment is being sought to unlock stalled residential and mixed-use developments. This should be on the basis of full financial disclosure by stakeholders with appropriate safeguards for commercial confidentiality.[6]

4.3.4 The HCA is promoting collaborative working between stakeholders. Good practice will include in engendering common stakeholder understanding of the key variables in the development viability models.

4.3.5 Where stakeholders to the planning process choose to take this approach it will be essential that their business planning tools are adequate. The approach to development appraisal which can support a shared approach to viability needs to provide:

- **Transparency** – If the parties are to take a truly collaborative approach it is clear that a transparent tool, the accuracy and results of which all sides accept, will be fundamental. It goes without saying that there should only be one shared viability model.
- **Clarity on drivers** – To develop the parameters of a deliverable solution there will need to clarity on the drivers for each party and acknowledgement as to what each party needs from the scheme.
- **Clarity on returns** – Linked to the above point there should be visibility for all parties on what each party takes away from the deal (which will include financial & non-financial outputs).
- **Risk & reward share** – The tool will need to incorporate the agreed risk and reward share and provide an equitable deal in this respect. Return sharing will follow risk sharing.

4.3.6 The key to preventing challenges and ensuring cohesion between all parties involved in the development process is to engage stakeholders at the viability assessment stage. How do we establish a mechanism that ensures that developers, RSLs and other stakeholders will have bought into the approach, the assumptions and the findings of the study?

4.3.7 The challenge is to engage stakeholders in the process whilst retaining overall control. The contrasting perspectives and agendas of the respective stakeholders could easily place a burden on the study making the process onerous and convoluted. To avoid this it is beneficial to hold stakeholder consultation workshops at two key points in the viability process.

Stakeholder Consultation 1- Viability Modelling Assumptions

4.3.8 All of the inputs and assumptions should be agreed and discussed in the assumptions workshop ensuring a balanced and evidenced based approach. The workshop could include developers, Housing Associations and landowners if considered appropriate.

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[6] HCA Good Practice Note Investment and Planning Obligations: Responding to the downturn, July 2009

4.3.9 The outputs of any viability modelling exercise are always dependant upon the quality and accuracy of the inputs. The key assumptions / variables include:

- Unit types and sizes;
- Unit Mix– By type and tenure;
- Build costs – including assumptions relating to build standards;
- Site preparation / site abnormal costs;
- S106 / planning obligations;
- Sales values;
- Developer profit; and
- Affordable housing assumptions / Grant levels / Sale price to RSL.

4.3.10 The purpose of a stakeholder workshop at this stage is to discuss the assumptions and the implications they have on viability. The list above shows the number of assumptions that need to be made in assessing viability. Engaging with key stakeholders in the development industry not only improves the accuracy of assumptions it will also add transparency to the process and mitigates the risk of challenge.

4.3.11 The end result will be a series of assumptions that all stakeholders are confident provide a sound evidence base.

Stakeholder Consultations 2 - Draft Policy Recommendations

4.3.12 A second stakeholder consultation could be held at the draft policy stage of the report. The purpose of this session is to test the likely policy recommendations emerging from the viability modelling with the key stakeholders.

4.3.13 Such a workshop is an important opportunity to demonstrate to key stakeholders, transparently, how the assumptions and modelling are translated into policy recommendations. Involvement of the stakeholders at this stage will mitigate the chances of the core strategy and supporting documentation being challenged.

4.4 Grant Availability

4.4.1 The availability of grant can have a powerful impact on viability by increasing the sum an RSL can pay a developer for the affordable housing units.

4.4.2 In most areas, social rented housing is unlikely to be viable without Social Housing Grant. This may also be true of intermediate housing. It is also important to explore with the HCA locally the proportion of sites which can expect to attract grant over the plan period, and the likely current and future grant levels.

4.4.3 It is our experience that across England, grant levels tend to be lowest in higher value areas where there are large areas of new Greenfield housing. This is an expected conclusion given the relative costs of Greenfield versus brownfield development.

4.4.4 HCA stated policy (set out in the Housing Corporation bid guidance for the 2008-11 funding programme) is that grant will only be provided on S106 sites for schemes where ‘additionality’ can be demonstrated. For example this could include the provision of bigger units, a higher proportion of social rented housing, or affordable housing built to higher standards. In practice the HCA has allocated substantial sums of funding to S106 sites and this has generally been based on the claim that the affordable housing element could not be provided without it. We also know that while there is a great deal of nil grant S106 social rented and shared ownership housing in the South East and East Anglia, this is not always the case in Thames Gateway, where remediation and infrastructure costs can be very high .

4.4.5 Since the market downturn there has been a more general acceptance by the HCA that many sites will need grant to support the provision of affordable housing by a developer and that the need for this should be demonstrated to them through the use of a viability model. This is reflected in the advice in the HCA good practice note July 2009 previously quoted.

4.4.6 Typical information a local authority would need to explore with potential funders are:

- Historically, what has been the role of grant in the funding of RSL projects on sites secured through the planning system - so-called S 106 sites?
- How common has nil grant affordable housing been in the TGSE area?
- Do HCA have a protocol with the Local Authorities on which schemes HCA are likely to fund and what the level of grant would be, both for social rented housing and for intermediate tenure schemes?
- What stage has the dialogue between local authorities and the HCA regarding future investment plans, which the HCA has called the 'Single Conversation' reached with each local authority within TGSE?
- Is there any current understanding between HCA and the local authorities on the likely annual level and scale of funding available in the TGSE area over the next few years?
- Have any assumptions been made about what the average grant amount per unit is likely to be (for both RSL and intermediate tenure)?
- For how long is it possible to estimate the level of grant funding will be available for RSL schemes on S106 sites in TGSE?
- What about the funding needs of the major strategic sites with significant infrastructure requirements? Are they being treated differently?
- Does HCA have any other funding streams which might be relevant to the brownfield sites in Thurrock? For instance the Kickstart Programme?

4.4.7 From discussions with HCA on these issues, we have learned that grant levels have fluctuated quite considerably since 2004 in the Eastern Region. The expectation is that current market circumstances will result in them rising.

TRIBAL

5 Delivery / Negotiating s106 contributions

5.1 Pragmatism and Flexibility

5.1.1 Negotiating affordable housing provision and s106 contributions is particularly difficult in the current climate. Negotiation is likely to be needed on sites with planning consent, sites where a planning application is to be made, and phased sites.

5.1.2 A clear, evidence based viability assessment in an agreed format is needed as the basis of negotiation.

5.1.3 A discussion on timing of obligations will also be necessary, particular in relation to deferring contributions. Councils have to be pragmatic about what they are asking for, such as by making their agreements more flexible to accommodate changing circumstances, or deferring or discounting payments in anticipation of an upturn in the building market. However, time limits to any ‘compromise’ should be set to allow for market recovery.

5.1.4 One approach is to work on a ‘deferred payment’ basis, with developers paying a certain amount up front, and the full sum later on, sometimes in several installments. The risk is that if contributions are deferred, the facility or affordable housing as part of the s106 agreement is never delivered. The question of risk is something Councils should discuss with partners such as HCA to find ways of covering the risk in some way.

5.1.5 There is a need for a regular review of planning policy in response to changing market conditions.

5.2 Proactive planning

5.2.1 In general, Local Authorities can increase the chances of meeting affordable housing targets and delivering much needed housing in a number of ways, including increasing knowledge of development economics and development appraisal, being consistent in what they are asking for, and creating a sense of certainty so that developers know where they stand.

5.2.2 Due to the market downturn, developers are unlikely to provide the number of affordable units planned, either from lack of development activity or as a result of the negotiation of lower percentages of affordable housing on viability grounds. Therefore there needs to be an assessment of other ways of maximising affordable housing delivery through housing and planning led approaches.

5.2.3 Land potential should be reviewed by the local authority and strategies such as land assembly and CPO could be explored. This may include the sale of publically owned land for RSL or Council led development, or the consideration of sites for change of use to allow affordable housing development where private housing development may not otherwise be permitted.

5.2.4 The capacity of RSLs for development in the area and their appetite for intermediate housing such as shared ownership, where values have been affected by the downturn, should be assessed and plans for joint working developed.

TRIBAL

6 Alternative Investment Models

6.1.1 RSLs and the private sector have over recent years been the main providers of housing. The Financial Business Plans of some RSLs and many developers/housebuilders have had a negative impact following the property market downturn. RSLs have in the past increased their shared ownership development programmes as well as some building and selling private sale properties through subsidiaries. The reduced capital receipts on shared ownership units and private sale units have affected some RSLs more than others. Developers/Housebuilders have of course been affected dramatically with resulting rationalisation, redundancies and significant reductions in share prices.

6.1.2 The way in which RSLs and the private sector approach housing development in the future may be different following the difficulties they have faced through this downturn in the property market. Different delivery structures, some of which we have seen already may become commonplace in the future as shared risk, skills and resources may be considered more appropriate for housing development delivery.

6.1.3 Furthermore, in recent years local authorities in England have been encouraged to consider a range of alternative investment models that will deliver the scale and quality of affordable and or / growth housing required in an area, as well as engaging with the private sector to deliver regeneration and economic development projects. These models to date have been driven by local authorities or other public bodies that have land assets that they wish to use for housing and community development. Essentially the majority of the models involve using the land assets of the local authority in a special purpose legal vehicle designed to lever private sector development finance into a scheme.

6.1.4 Alternative investment models have been considered mainly because:

- The development is strategic and the local authority wishes to maintain a level of control over what is developed, the scale and the timing of development.
- The level of risk associated with the development suggests that disposal of land to the private sector alone will not guarantee development in a realistic timeframe. By reducing up front risk associated with land acquisition and sharing risk and reward the scheme can become viable and can be delivered more quickly.
- Value/uplift capture and retention – a proportion or all of the value of a scheme (whether it can be rising land value or development surplus) can be retained by the local authority and invested in other schemes – enabling downstream viability for other schemes etc.
- The scheme involves the renewal of large areas of social housing and the normal market mechanisms are difficult to apply.
- Access to funding – the involvement of a local authority can provide improved access to other form of public finance to improve viability.
- In development/regeneration projects risks can be better dealt with by the private sector.

6.1.5 Each of these investment models involves local authorities being exposed to some degree of additional risk. That risk is primarily financial and related to success of the development, the choice of private sector partners and the funders that are part of any agreement. Local authorities have been and remain cautious about exposure to risk of this type and proposals are scrutinised carefully by government. For these reasons the transaction costs of establishing investment models of this type can be extensive, expensive and time consuming. However more recently, driven by the unprecedented effects of the recession on the housing market, there have been calls for local authorities to be more creative and innovative in their risk taking to help stimulate the market and achieve public policy housing objectives. *The All Party Urban Development Group report* on Regeneration in the Recession is a useful document for further reading in this respect.

6.1.6 The most commonly discussed models for development involving local authority land for housing are Local Asset Backed Vehicles (LABV) English Partnerships, now HCA, established 14 pilot LABVs across the country. In LABVs, local authority land assets are used to lever investment from the private sector. They bring together a range of public and private sector partners in order to pool finance, planning powers, land and expertise, to ensure a sensible balance of risk and return for all partners and to plan and deliver projects more strategically. The complexity of establishing the investment vehicle means that significant land assets are required to justify it and for the proposal to be attractive to the private sector. In practice very few of these are fully operational as yet.

6.1.7 There is no uniform method of designing LABV arrangements but the standard process requires a Local Authority to identify a portfolio of assets and/or regeneration projects. Once a private sector partner is identified the collaboration is then formalised into one company with one governance structure. Examples are Joint Ventures and Local Housing Companies.

6.1.8 It is anticipated that the parties will bring the following:

Private Sector Investors	**Local Authorities**	**Developers**
Finance	Land Assets	Land Assets
Development Funding Expertise	Access to inclusive stakeholder engagement	Project Design and Delivery Expertise
Risk Management	Statutory Planning and Regulatory Powers	Finance

6.1.9 The other most commonly used mechanisms for delivery of schemes also include the use of Public Private Partnerships in which public authorities enter into an arrangement with private sector bodies to Design, Build Finance Operate (DBFO) a building or service. The Private Finance Initiative (PFI) was originally identified for stock improvement but has moved on to new build provision and delivery.. The recession has increased the levels of risk associated with these investment vehicles.

6.1.10 The principle of a good PFI scheme is where the transfer of risks to the private sector who can better deal with them is achieved. Most beneficial PFI schemes have a capital investment element and service provision element, both of which are paid for by the Local Authority over a long term contract. PFI Credits are then available from the Government to support the capital element.

6.1.11 In April of this year, the Government launched a new initiative to tackle the slow down of the delivery of affordable housing. It offered a pot of £150million to allow Local Authorities to submit bids for funding to build affordable housing properties on their own land. This pot of funding was increased in June to a total of £350milion.

6.1.12 Whilst there is a value to the land which Local Authorities contribute, it is represented as a nil cost when calculating the total development scheme costs. In this respect, the grant sum is competitive against normal RSL development projects where there is normally a land cost included and therefore a requirement for a higher grant amount.

6.1.13 There have been two bidding rounds for this funding and the take up appears to be high. However, the timescales set down in the criteria in terms of the properties being built are challenging and so it remains to be seen how successful this initiative will be.

6.1.14 More recently major schemes and growth schemes where the locally authority does not own land are focussing on mechanisms that can find ways to forward fund infrastructure to de-risk developments and enable them to be brought forward more quickly. The most notable of which are as follows:

- **Regional infrastructure Funds** are being considered by RDAs as a loan facility to help fund private sector contributions to development projects. In some cases the loans are only partly repayable and so will increase viability as well as cashflow. The funds are created by top slicing budgets and are aimed at the timely facilitation of infrastructure. The capital investment can be partly recovered from Section 106 contributions and the Community Infrastructure Levy.

- **Joint European Support for Sustainable Investment in Cities (JESSICA)** –is part of the EU structural funding regime for the period 2007-20013. It allows RDAs to use a proportion of Fund allocations to create an urban development fund for use of guarantees, equity or loans to the private sector for projects delivering lasting improvement in the economic, physical, social and environmental conditions of a city. The funds can be recycled over time and could be matched with Regional Infrastructure Funds as above. The perceived benefits of this initiative are:

  - Funds can be recycled.
  - The initiative will lever in private sector finance.
  - Flexibility.
  - The initiative will bring in expertise and creativity from the banking sector.

- **Accelerated Development Zones** - these are at an early stage of discussion and would enable local authorities to use prudential borrowing to forward fund infrastructure based on future local increased tax income. This is based on an US model and carries some risk in terms of the outcome. The future of this initiative is uncertain due to tightened lending criteria and the Empty Property Rates legislation.

7 Thames Gateway South Essex Housing Viability Seminar

7.1.1 This chapter deals with housing viability issues that were raised at the Tribal Housing Viability Seminar held on October 28th 2009 with Housing, Regeneration and Planning partners in the sub region.

7.1.2 Presentation slides from the seminar can be found in Appendix A.

7.1.3 It is estimated that in excess of 40,000 new homes are required to be delivered in South Essex by 2021. This is a significant number and the challenge will be ensuring that they offer a mix of housing which is affordable and designed to meet the needs of existing and future residents.

7.1.4 The concern for some professionals however, who are working to deliver these new homes is whether the required infrastructure will be in place to support this housing growth. The term infrastructure is normally used to define the requirements that are needed to make places function. Infrastructure is commonly split into three main categories:

- **Physical:** the systems and facilities that house and transport people and goods, and provide services e.g. transportation networks, housing, energy supplies, water, drainage and waste provision, ITC networks, public realm

- **Green:** the physical environment within and between our cities, towns and villages. A network of multi-functional open spaces, including formal parks, gardens, woodlands, green corridors, waterways, street trees and open countryside.

- **Social & Community:** the provision of community facilities (education, healthcare, community centres, sports & leisure facilities), local networks, community groups, small scale funding to assist fund local projects, skills development and volunteering.

7.1.5 Infrastructure improvements will be vital for the growing population. The infrastructure will need to provide facilities for the area and communities to function and to ensure the creation of sustainable communities.

7.1.6 This new infrastructure will be expensive and the concern is that the housing will be delivered before adequate and necessary infrastructure is in place, because the Government cannot afford to forward fund the cost. This concern has increased as the property market has taken a downturn. Potential financial contributions from profits on sales of private sector housing to fund infrastructure costs, looks bleak in the current depressed market.

7.1.7 Other issues that were raised during the seminar group discussions relate to what measures could be taken to improve housing delivery in the current and future market. These suggested measures are:

- More joint working between RSLs – this would reduce competition (and as a consequence land value and timescales) and would allow risk to be shared.

- Local Authorities should share more information with RSLs/partners – for example give details of their own pipeline schemes/opportunities.

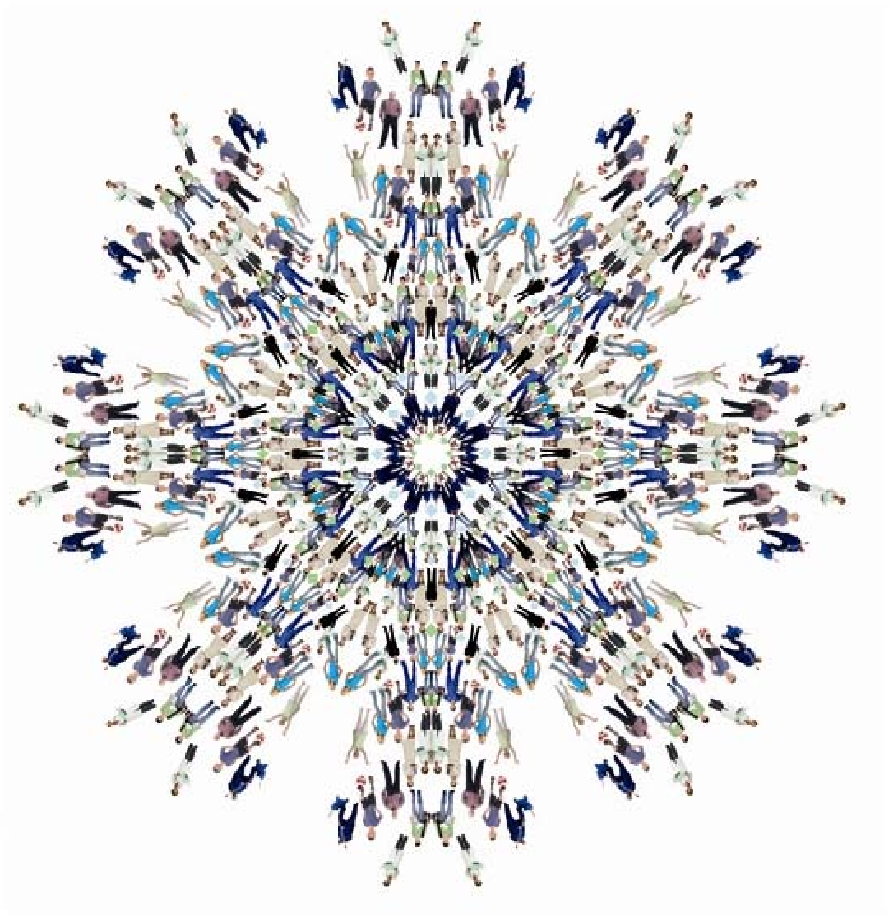
- The provision of a single investment plan – combining different initiatives regionally giving a more co-ordinated approach.

- Joining services together – planning, transport, housing giving a more strategic and co-ordinated approach – the development of a website demonstrating funding pots and initiatives.
- Bring lenders to the table as partners.
- HCA to be more open about land availability.
- Increase the use of CPO powers.
- RSLs should review all of their current landholdings to identify potential opportunities.
- HCA should have the role of a conduit for other funding routes.
- Local Authorities should as part of their Asset Management role, identify land opportunities for sale or joint development.

Appendix A: Housing Viability Seminar 28th October 2009 - Presentation Slides

TRIBAL

Improvement East



Housing Viability and Delivery

Thames Gateway South Essex

Services for life

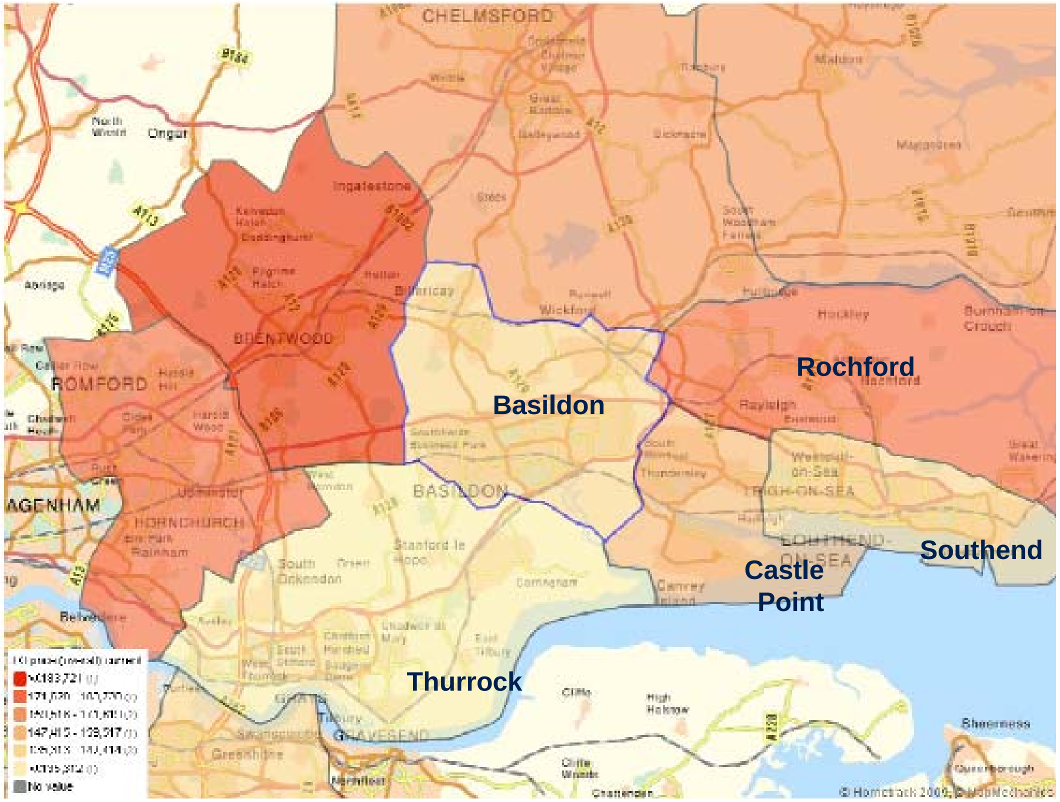
Thames Gateway South Essex –context

Thames Gateway South Essex: Context

- Single functional sub-regional housing market
- Similar characteristics – house prices, socio economic profile
- Sub region part of TG Growth Area / national regeneration priority
- Basildon, Southend and Thurrock urban area are KCDC; sub-region a Priority Area for Regeneration and Regionally Significant Employment Location in the RSS.
- Main housing sub markets are three primary areas / economic hubs of Basildon, Southend and Thurrock.

TRIBAL

TGSE Context (2)



- Current house prices low
- Affordable housing delivery across sub region averaged 22% 2001-08 but has dropped off
- Stronger in some parts of sub region than others
- Housing need most acute in Thurrock and Basildon
- Overall 54% of households cannot meet their needs in the market – pre recession figure
- Development grinding to a halt as a result of the credit crunch?
- We need to understand development viability and support delivery where possible

TRIBAL

TGSE Growth Plans

VIABILITY ASSESSMENT:

Principles

TRIBAL

Development viability

Modelling viability is useful for:

- Planning policy development – required to support affordable housing planning policy
- Development control - Informs negotiations with developers on whether current or proposed requirements are reasonable
- Gaining an understanding of ‘delivery issues’

TRIBAL

Viability – a definition

‘*Affordable housing delivery from planning permissions is viable when the cost to the developer in the form of a* ***discounted price****, to the affordable housing provider can be accommodated in the scheme economics,* ***without undermining profitability****, and is reflected in the* ***price paid for the land****’*

- HCA good practice note July 2009

TRIBAL

Appraisal Tools

- Existing Approaches
  - HCA Economic Appraisal Tool
  - Three Dragons
  - GLA toolkit
- All use a residual land value method
- The model is simple: the challenge is in making the correct assumptions

TRIBAL

Development Appraisal

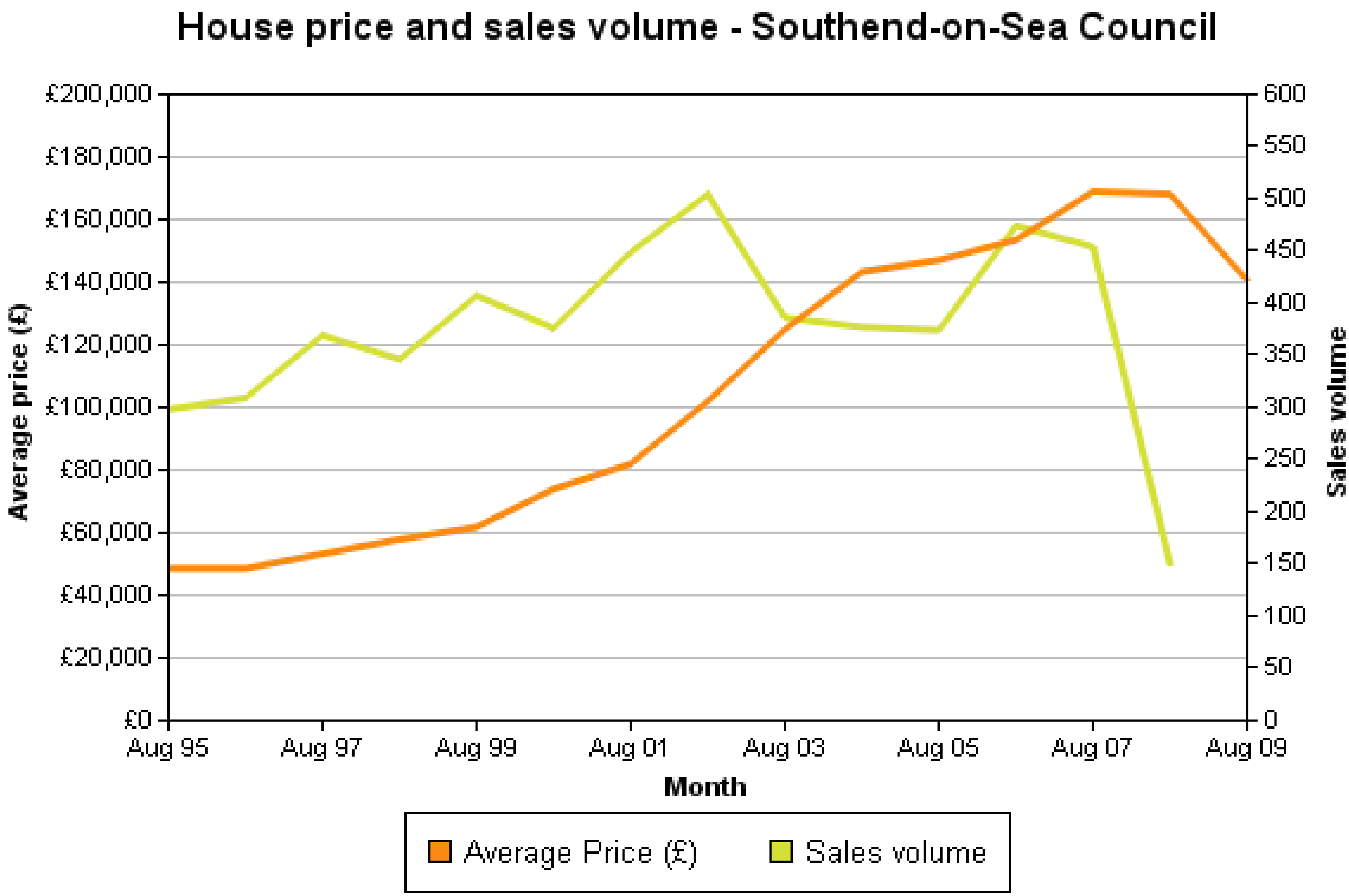
- Residual Land Value (RLV)
- Residual valuation principle

RLV = Finished open market value – Build Costs – Profit etc

- Example

Development Value	**250,000**
Build Costs	
Infrastructure	20,000
Construction	100,000
Total	120,000
Profit & Fees etc	
Fees	25,000
Interest	10,000
Profit	43,750
Total	78,750
Residual Land Value	51,250

Value of private housing



TRIBAL

Value of affordable housing

- Affordable rent – target rent levels, aimed at those in priority need
- Intermediate – products aimed at those not eligible for the above but who cannot afford to buy:
  - New Build Homebuy (shared ownership) – part buy, part rent
  - intermediate rent – maximum of 80% market rent level
- **Values**
  - Affordable and intermediate rented = **Capitalised net rent + grant**
  - New Build Home Buy = **First tranche equity stake sold + Capitalised rent on unsold equity + grant**
  - Figures enhanced by RSL reserves where available!

TRIBAL

Assessing viability

- RLV calculation including affordable housing:

  Income from private sale housing
  + Income from RSL for affordable housing (given certain tenure, grant etc)

  = total scheme value

  Less construction costs, fees and profit
  = RLV (maximum developer can pay for land)

- Compare RLV to benchmark land value to assess viability

TRIBAL

Modelling the market

- Selecting appropriate benchmark land values is key :
  - Peak historic values not appropriate – although landowners may aspire to achieve them
  - Housebuilders have had to write landbanks down to price paid – or an RV based on current dev prospects
  - HCA all too aware that maintaining 2007 expectations of land value in 2009 may mean development not viable
- Is there any point in modelling values at the bottom of the market? Suggest a mid point between peak and trough
- How can model adapt to market changes?

TRIBAL

Supporting developer negotiations

- Negotiating in the current climate on:
  - Sites with planning consent
  - Sites where a planning application is to be made
  - Phased sites

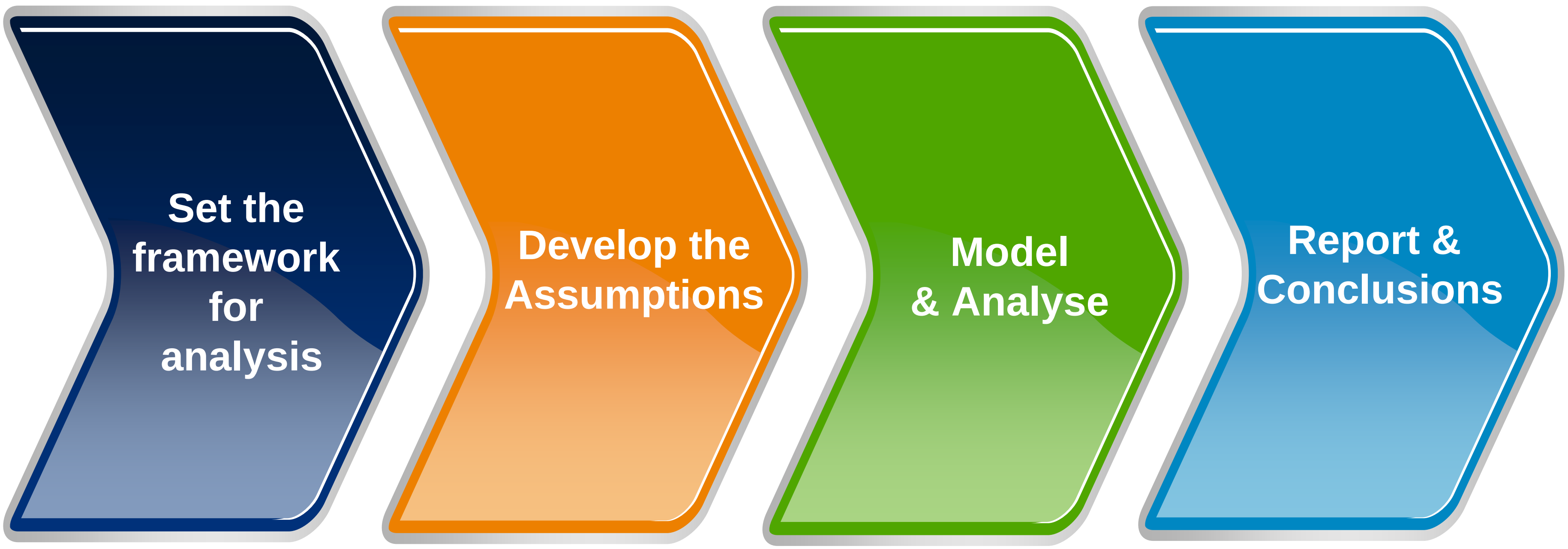
- Need clear, evidence based viability assessment in agreed format
- Timing of obligations – can they be deferred?
- Time limits to any ‘compromise’ to allow for market recovery
- Need for regular review of planning policy in response to changing market conditions
- Consider options for additional HCA funding

VIABILITY ASSESSMENT:

Modelling

TRIBAL

Our Approach



TRIBAL

Set the framework for analysis

Site	Site Type		Site Size				Housing Market Demand	
	Greenfield	Brownfield	Small	Medium	Large	Super	High / Medium	Low
1		✓	✓				✓	
2		✓	✓					✓
3		✓		✓			✓	
4		✓		✓				✓
5		✓			✓		✓	
6		✓			✓			✓
7		✓				✓	✓	
8		✓				✓		✓
9	✓		✓				✓	
10	✓		✓					✓
11	✓			✓			✓	
12	✓			✓				✓
13	✓				✓		✓	
14	✓				✓			✓
15	✓					✓	✓	
16	✓					✓		✓

- Matrix Approach – archetypes reflect range of development scenarios
- Site Categories
- Site selection

TRIBAL

Develop the assumptions

- Key appraisal assumptions
  - Build costs
  - Site preparation / site abnormal costs
  - S106 / planning obligations
  - Sales values – new housing
  - Affordable housing assumptions
  - Grant level
  - Benchmark land values
- Stakeholder Workshop

Affordable housing assumptions

- Percentage – units, habitable rooms or floor area?
- Mix of unit sizes – what does housing needs data show?
- Tenure – specify the balance of rent and intermediate
- Standards – HCA standards? Space standards? Code for sustainable homes level?
- Affordability – maximum income levels for shared ownership?
- Sale price to RSL– defined? nil land value? Cost per metre?

INPUT SHEET 2 - RESIDENTIAL VALUE & COST ASSUMPTIONS

RESIDENTIAL VALUE ASSUMPTIONS

Base Value

Affordable Housing Tenure 1: Social Rented

Type of Unit	Rent per Unit per Week (£)	Rent per Unit per Annum (£)
Studio	£66.25	£3,445
1 Bed	£76.86	£3,997
2 Bed	£85.90	£4,467
3 Bed	£96.93	£5,040
4 Bed	£105.98	£5,511
5 Bed		
2 bed house		

Management Costs (% of rent)	12.00%	(% of gross rent per annum)
Voids / bad debts (% of rent)	4.00%	(% of gross rent per annum)
Repairs Fund (% of rent)	18.00%	(% of gross rent per annum)
Yield (%)	6.25%	(to capitalise the net rent)

	Start Month	End Month	
Timing of Affordable Housing Tenure 1 Purchase Payment	15	27	(whole number, minimum o

Affordable Housing Tenure 2: Intermediate - Shared Ownership

Type of Unit	Total Unit Capital Value (£ psm, NIA)	Rent per Unit per week of rented share (£)
Studio	£3,090	£0
1 Bed	£3,090	£46
2 Bed	£2,900	£63
3 Bed	£2,900	£78
4 Bed	£2,900	£101
5 Bed	£2,900	£120
Other	£2,900	£70

Owner-occupied share (%)	40.0%		
Unsold Equity Rent Per Annum (%)	2.75%	(Housing Corporation Limit of 2.75%)	
Management Costs (% of rent)		7.00%	(% of gross rent per annum
Voids / bad debts (% of rent)		2.50%	(% of gross rent per annum
Repairs Fund (% of rent)		0.00%	(% of gross rent per annum
Yield (%)		6.25%	(to capitalise the net rent)

	Start Month	End Month	
Timing of Affordable Housing Tenure 2 Purchase Payment	15	27	(whole number, minimum o

Affordable Housing Tenure 5: Intermediate Rent

Type of Unit	Rent per Unit per Week (£)	Rent per Unit per Annum (£)
Studio	£0.00	
1 Bed	£108.16	£5,624
2 Bed	£143.52	£7,463
3 Bed	£152.88	£7,950
4 Bed	£172.64	£8,977
5 Bed	£182.00	£9,464
Other	£0	

Management Costs (% of rent)	12.00%	(% of gross rent per annum)
Voids / bad debts (% of rent)	4.00%	(% of gross rent per annum)
Repairs Fund (% of rent)	18.00%	(% of gross rent per annum)
Yield (%)	6.25%	(to capitalise the net rent)

	Start Month	End Month	
Timing of Affordable Housing Tenure 5 Purchase Payment	15	27	(whole number, minimum o

Open Market Values

		Capital Value (£ psm)
Open Market Housing Type 1:	Flats and Apartments	£3,090
Open Market Housing Type 2:	Terraced Houses	£2,900
Open Market Housing Type 3:	Semi-detached Houses	£2,900
Open Market Housing Type 4:	Detached Houses	£2,970
Open Market Housing Type 5:	-	

	Month	
Timing of First Open Market Housing Sale	15	*(whole number, minimum o*
Timing of Last Open Market Housing Sale	39	*(whole number, minimum o*

Overall Scheme End Date (this must be completed)

	Month	
Final End Date of Scheme - **scheme built and fully let/sold**	40	*(whole number, minimum o*

Social Housing Grant & Other Funding

		Grant per unit (£)
Affordable Housing Tenure 1:	Social Rented	£44,500
Affordable Housing Tenure 2:	Intermediate - Shared Ownership	£16,200
Affordable Housing Tenure 3:	Intermediate - Discounted Market Sale	
Affordable Housing Tenure 4:	Intermediate - Other Type of Shared Ownership / Shared Equity	
Affordable Housing Tenure 5:	Intermediate Rent	£16,200

	Timing of 1st Payment	Timing of 2nd Payment
Timing Social Housing Grant Paid	15	27

BUILDING COST, MARKETING COST & SECTION 106 ASSUMPTIONS

		Building Costs - Gross (£ / sq m)	Net to Gross Ratio for Building Costs (%)*
Affordable Housing Tenure 1:	Social Rented	£1,121	100%
Affordable Housing Tenure 2:	Intermediate - Shared Ownership	£1,130	100%
Affordable Housing Tenure 3:	Intermediate - Discounted Market Sale	£1,130	100%
Affordable Housing Tenure 4:	Intermediate - Other Type of Shared Ownership / Shared Equity	£1,130	100%
Affordable Housing Tenure 5:	Intermediate Rent	£1,130	100%
Open Market Housing Type 1:	Flats and Apartments	£1,119	80%
Open Market Housing Type 2:	Terraced Houses	£863	100%
Open Market Housing Type 3:	Semi-detached Houses	£922	100%
Open Market Housing Type 4:	Detached Houses	£1,019	100%
Open Market Housing Type 5:	-		

** The ratio is typically 70% - 85% in blocks of flats to reflect the difference between GIA & NIA (ie common parts such as lifts, stairs, corridors etc) and 100% in houses which have no common parts*

	Building Costs (£ / car parking space)	
Residential Car Parking Building Costs (£ / car parking space)		

	% of Building Costs	
Building Cost Fees % (Architects, QS etc)	10.00%	*(typically around 10%)*
Building Contingencies (% of Building Costs)	5.00%	*(typically around 5% for new*

Section 106 Payments (£) *	Cost (£)	Month of Payment
Infrastructure / Public Transport	£725,900	15
Community Facilities		15
Public Realm / Environment		15
Health		15
Facilities		15

* *This section excludes Affordable Housing section 106 payments*

Site Abnormals (£)		Cost (£)	Month of Payment
Infrastructure Costs		£0	8
Contamination Costs		£57,750	8
Demolition Costs		£92,400	8
Other Costs		£0	8
Site Specific Sustainability Initiatives**	**EITHER**		8

Building Cost Percentage Increase (if any)		%
Site Specific Sustainability Initiatives (%)**	**OR**	
Wheelchair provision (%)		
Code for Sustainable Homes (%)		4.08%
Intermediate Spec		

** *Only one sustainability initiatives box should have a value / percentage.*

OTHER COSTS

SITE ACQUISITION COSTS

	%	
Agents Fees (% of site value)	1.00%	*(typically around 1%)*
Legal Fees (% of site value)	0.75%	*(typically around 0.75%)*
Stamp Duty (% of site value)	4.00%	

	Cost (£)	Month of Payment
Other Acquisition Costs (£)		3

FINANCE COSTS

Arrangement Fee (£)	£60,000	
Interest Rate (%)	£0	*(typically around 1.5% to 3%*
Misc Fees - Surveyors etc (£)	£40,000	

Marketing Costs

Affordable Housing Marketing Costs

	Cost (£)	Timing (month)
Developer cost of sale to RSL (£)	£48,000	27
RSL on-costs (£)	£230,948	27
Intermediate Housing Sales and Marketing (£)	£28,000	27

Open Market Housing Marketing Costs

Sales Fees (agents fees & marketing fees) - %	6.00%	*(typically around 6%)*
Legal Fees (per Open Market unit) - £	£650	*(typically around £600 per u*

BUILDING PERIOD

	Timing (month)	
Construction Start	3	*(whole number, minimum of 0, maximum of 60)*
Construction End	27	*(whole number, minimum of 0, maximum of 60)*

DEVELOPER'S 'PROFIT' (before taxation)

	% of Housing Capital Value	
Open Market Housing (%)	17.50%	*(typically around 15%)*
Affordable Housing (%)	6.00%	*(typically around 6%)*

TRIBAL

Tribal Input Sheet

Inputs

Basic Site Details

Site Address	Example
Site Reference	
Scheme Description	Medium brownfield high demand high density
Date	08/09/2009
Site Area (hectares)	0.77
Author & Organisation	Jackie Strube - Tribal
Housing Corporation Officer	N/A

Typology Selection (select from drop down options)

Site Size	Medium
Demand Type	High / Medium
Site Type	Brownfield
Density Type	High

Unit Mix

Total Units 153

Aff HR %	30%

Check		
Total Units Input	153	CORRECT

Open Market Units 68% 104.7

Affordable Units

		Suggested	Actual
% Affordable	32%	48.3	48
Social Rented	70%	33.8	34
Shared Ownership	15%	7.2	7
Intermediate Rented	15%	7.2	7
			48

Affordable Units

	Studio	1 Bed	2 Bed Flat	2 Bed House	3 Bed	4 Bed	5 Bed	
Social Rented (Suggested Split)	0.0	15.2	10.1	5.1	3.4	0.0	0.0	
Social Rented (Actual Split)		15	10	5	4	0	0	34
Shared Ownership (Suggested Split)	0.0	3.3	2.2	1.1	0.7	0.0	0.0	
Shared Ownership (Actual Split)		3	2	1	1	0		7
Intermediate Rent (Suggested Split)	0.0	3.3	2.2	1.1	0.7	0.0	0.0	
Intermediate Rent (Actual Split)		3	2	1	1	0		7

Open Market Units

	Studio	1 Bed	2 Bed	3 Bed	4 Bed	5 Bed	
Flats & Apartments	0.0	36.7	36.7	10.5	0.0	N/A	
		37	37	10		N/A	84
Terraced Housing	N/A	n/A	0.0	0.0	0.0	N/A	
	N/A	N/A	0	0	0	N/A	0
Semi-detached Housing	N/A	N/A	10.5	10.5	0.0	0.0	
	N/A	N/A	11	10	0	0	21
Detached Housing	N/A	N/A	N/A	0.0	0.0	0.0	
	N/A	N/A	N/A	0	0	0	0
Total	0	37	48	20	0	0	105

TRIBAL

Scheme Description	Medium brownfield high demand high density
Date	08/09/2009
Site Area (hectares)	0.77

Residential Values

Affordable Housing Tenure 1: **Social Rented**

Total Capital Value of Affordable Housing Tenure 1	**£1,317,664**
Total Capital Value of Affordable Housing Tenure 2	**£828,673**

Affordable Housing Tenure 5: **Intermediate Rent**

Total Capital Value of Affordable Housing Tenure 5	**£419,747**
TOTAL CAPITAL VALUE OF ALL AFFORDABLE HOUSING (EXCLUDING SHG & OTHER FUNDING)	**£2,566,084**

Social Housing Grant

TOTAL VALUE OF SOCIAL HOUSING GRANT	**£1,739,800**
TOTAL CAPITAL VALUE OF ALL AFFORDABLE HOUSING (INCLUDING SHG & OTHER FUNDING)	**£4,305,884**

Open Market Housing

TOTAL CAPITAL VALUE OF OPEN MARKET HOUSING	**£19,283,610**
TOTAL CAPITAL VALUE OF RESIDENTIAL SCHEME	**£23,589,494**
TOTAL VALUE OF SCHEME	**£23,589,494**

Residential Building, Marketing & Section 106 Costs

Total Building Costs	**£11,907,536**

OTHER SITE COSTS

Total Other Site Costs	**£2,721,718**
Total Marketing Costs	**£1,532,214**
TOTAL DIRECT COSTS:	**£16,161,467.96**

Finance (finance costs are only displayed if there is a positive residual site value)

Total Finance Costs	**£1,440,900**

Developer 'Profit'

Total Operating Profit	**£3,528,597**

Residual Site Value

SITE VALUE TODAY	**£2,458,529**
EXISTING USE VALUE	**£770,000**
DIFFERENCE BETWEEN SITE VALUE AND EXISTING USE VALUE	£1,688,529
Site Value per hectare	£3,192,895

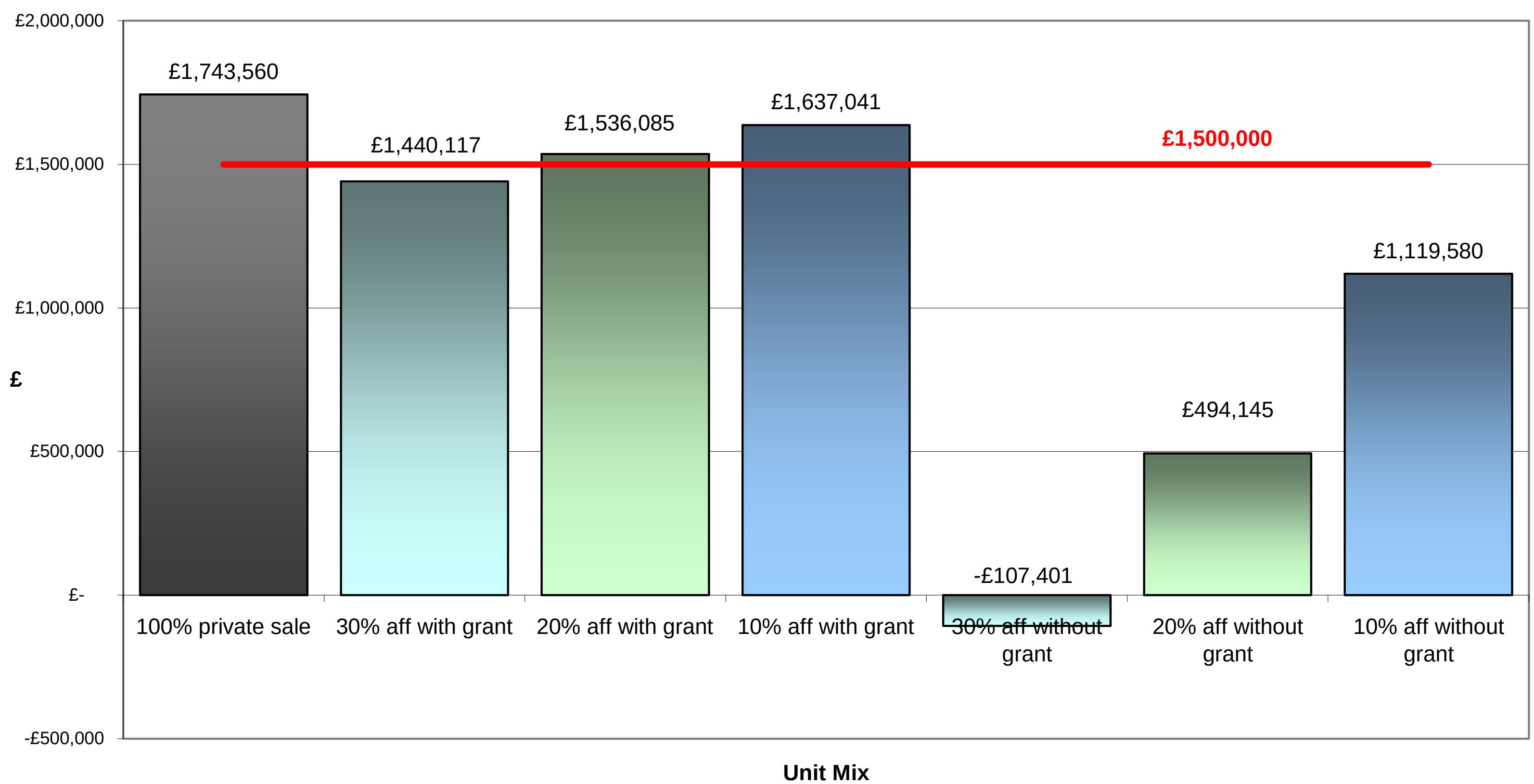
TRIBAL

Model Outputs - Example

132 - Project X

Location	Suburban Brownfield
Size	Large
Units	100
Density	Low
Demand Type	Medium Demand

	Benchmark Land Value
	100% Private Sale - Residual Land Value
	30% Affordable - Residual Land Value
	20% Affordable - Residual Land Value
	10% Affordable - Residual Land Value



Planning Policy Issues

Policy options – Issues to consider

- Viability will differ considerably between districts and within districts across TGSE
- The policy challenge is to deal with that variability in an efficient way, without losing the potential to capture the benefits of the uplift in value on the sites and locations where there is strong potential to secure benefits
- Grant levels are likely to be important in securing mixed tenure affordable housing development on sites with less market strength

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Policy options – issues to consider (2)

- Planning policy – set in PPS3: Housing
  - *'Local Planning Authorities should …set an overall (ie plan wide) target for the amount of affordable housing to be provided. The target should…reflect an assessment of the likely economic viability of land for housing within the area, taking account of risks to delivery and drawing on informed assessments of the likely levels of finance available for affordable housing, including public subsidy and the level of developer contribution that can reasonably be secured'.*
- Importance of getting policy right. Blyth valley etc
- Things to consider:
  - Borough wide targets?
  - or modified according to type and location of development?
  - Site size threshold?
  - In what circumstances will there be flexibility ?
  - How will the policy respond to market change?
  - Set higher target with flexibility to allow for short term market weakness ?

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Policy Options – Issues to consider (3)

Other considerations:

- Percentage - % target of all housing to be affordable
- Tenure mix - split between social rented and intermediate
- Subsidy levels - grant levels required to deliver viable development given a specific affordable housing percentage.
- Infrastructure contributions - the capacity of new development to support current and future policy infrastructure requirements. There will need to be a policy approach to these requirements in cases where site viability is at risk.
- Payments in lieu of affordable housing
- Market change - mechanisms for future review of policy.
- Role of Cascades – marginal situations / large strategic sites

- Process provides sound evidence base to produce recommendations on the viability of:
  - Proportion of affordable housing
  - Mix of affordable housing tenures
  - Providing affordable housing in different locations and on different site types
  - Threshold levels
  - Using commuted sums

INVESTMENT AND DELIVERY MODELS

RSLs

- RSLs with HCA funding – have been main providers of affordable housing and some have started to build for private sale.

Issues:

- RSLs have suffered as a result of market downturn
- Scale of future HCA programme is uncertain and there will be competing priorities.

LABVs

- Local Asset Backed Vehicles: new company created where local authority contributes land and other support for a return on the investment. May be in the form of Joint Venture or Local Housing Company

- Issues:
  - Complex to set up
  - Suitable for large programmes only
  - Local authority must have land to contribute (with value)

- Private Finance Initiative (PFI) – Private Public Partnership where partners share risk and reward, to ‘Design Build and Operate’ .Funding is provided through long term revenue subsidy by local authorities supported by PFI ‘credits’

Issues:

- Publicly owned land
- Needs to be large scale
- Complex to set up and manage

Local Authority New Build

- 2009 HCA Programme - New affordable rented housing on local authority owned sites to HCA standards. Land contributed for nil. £3.5billion programme in 2009 allocated via two bid rounds.

- Issues:
  - HRA reform may increase local authority capacity to develop
  - Can only deliver housing for rent at present

TRIBAL

Schemes to forward fund infrastructure

- **Regional infrastructure Funds** - RDAs acts as loan facility to help fund private sector contributions to development projects.

- **JESSICA** –is part of the EU structural funding regime for the period 2007-20013. It allows RDAs to use a proportion of Fund allocations to create an urban development fund to support private sector development.

- **Accelerated Development Zones** - would enable local authorities to use prudential borrowing to forward fund infrastructure based on future local increased tax income.