

## **AFFORDABLE HOUSING, THE DEVELOPMENT PLAN AND VIABILITY**

### **OPINION**

#### **Introduction and Summary**

1. I am asked by a number of London local authorities (“the LAs”) to give my opinion as to the correct approach to land value (“LV”) in viability assessments (“VAs”) concerning affordable housing (“AH”) provision.
2. I consider that the position is clear and has been most recently, correctly, reflected in the Mayor of London’s draft Affordable Housing and Viability Supplementary Planning Guidance 2016 (“the Mayor’s draft SPD”) and London Borough Development Viability Protocol November 2016 (“the Protocol”). Those documents approach the issue from a planning policy perspective. Approaching the same issues from basic principle and the requirements of s.38(6) of the Planning and Compulsory Purchase Act 2004 (“the 2004 Act”) yields the same answers.
3. An approach to land value in viability appraisals which did not “reflect” development plan policy requirements inevitably introduces a circularity which serves to undermine the achievement of those policies and, contrary to policy, increases land value by reducing AH. Whether this is the cause of the dramatic reduction in AH provision in recent years is unclear – there are many other factors in play - but a principled and s.38(6) compliant approach would treat AH requirements as a given cost to the development (just as are all other requirements and constraints on development) such that by definition and subject only to the benchmark land value issue, policy compliant AH will be viable.
4. On benchmark land value, the approach of the Mayor’s draft SPD is compelling. There are insuperable problems with relying on “open market value” because open market value has, by definition, developed (perhaps influenced by the RICS Guide 2012) in a way which does not properly reflect policy requirements. Alternative use value is a potential route to assessing BLV but there are a number of high hurdles which would need to be overcome such that in practice it will only be when detailed permission exists for the alternative, that it will provide a good basis for a BLV.
5. I address the questions posed in my Instructions as I go through the issues which, in my view, arise. I have not been asked to and do not advise on the specifics of London Plan or Local Plan policies.

#### **The Statutory Scheme: Development, Planning Permission and the Development Plan**

6. The planning system exists to control development in the public interest. Planning permission is required for development. Whether permission will be granted depends on overcoming physical or policy impediments to development.
7. Applications for planning permission are to be determined in accordance with the development plan unless material considerations indicate otherwise: s.38 (6). This provision creates a statutory presumption in favour of the policies contained in the adopted

development plan: *R (Cala Homes South Ltd) v. SSCLG* [2011] EWCA Civ 639; [2011] JPL 1458: per Sullivan LJ at [6].

8. Those policies will be formulated to reflect what development is and is not acceptable in the public interest (“the constraints”) or what specific provision to meet needs any particular development has to make (“the requirements”). Those policies either constrain or impose costs on the unfettered development (and thus value) of a particular site. Myriad examples could be cited but the most obvious constraints include: (1) green belt policy restricting the permissible form of development in a given area; (2) heritage considerations limiting the height or scale of buildings in a particular location; (3) environmental considerations requiring green corridors to be provided. The “requirements” may cover social, green or transport infrastructure, sustainable transport provision and AH. All of these policy constraints in the public interest will serve to determine the land value because they determine what, if any development, will be deliverable on a particular site.
9. In London, the development plan comprises (at least) the spatial development strategy of the Mayor (“the London Plan”) and the LA’s development plan documents (“DPDs”): s.36 (2). In formulating their DPDs, the LAs must have regard to national policy (s.19) and the DPDs must be in general conformity with the London Plan: see e.g. s.21A Town and Country Planning Act 1990 (“the 1990 Act”).
10. The interpretation of the policies is for the Courts: *Tesco Stores Ltd v. Dundee City Council* [2012] PTSR 983 @ [19-20].

#### **Affordable Housing need in formulation of the development plan and decision making**

11. A community’s need for AH is relevant to planning and a policy requirement to provide AH is a proper exercise of plan making powers and land use planning powers: see e.g. *R v Tower Hamlets LBC ex parte Barratt Homes* [2000] JPL 1050 @ at p.1055-6 and p.1060-1. This has the inevitable effect of depressing land value from what it would have been worth if AH was not a material planning consideration.

#### **The NPPF: Assessing the Need for AH and Planning to Meet the Need**

12. Paragraphs 47 of the National Planning Policy Framework (“the NPPF”), to which regard must be had under s.19 above, provides that:

***“To boost significantly the supply of housing, local planning authorities should:***

- ***use their evidence base to ensure that their Local Plan meets the full, objectively assessed needs for market and affordable housing.... so far as consistent with the policies in this Framework...”***

13. The central significance of paragraph 47 and the imperative to plan to meet need was emphasised in *St Albans City and District Council v. Hunston* [2013] EWCA Civ 1610; [2014] JPL 599 @ [6], [25 – 26]; and *Solihull MBC v. Gallagher Estates* [2014] EWCA Civ 1610; [2015] JPL 713 @ [9-10].
14. Paragraph 50 provides as follows:

***“To deliver a wide choice of high quality homes, widen opportunities for home ownership and create sustainable, inclusive and mixed communities local authorities should:***

- ***plan for a mix of housing based on current and future demographic trends, market trends and the needs of different groups in the community....***
- ***Identify the size, type, tenure and range of housing that is required in particular locations reflecting local demand; and***
- ***Where they have identified that affordable housing is needed, set policies for meeting this need on site....”***

15. Paragraphs 150 – 157 concern the Local Plans. They should be “aspirational but realistic” [154] and should include strategic policies “to deliver the homes....needed in the area” [156]. I regard these paragraphs as central to all that follows. The government requires planning policy in the public interest to meet all AH need including through imposing AH on housing sites. This is a central and inescapable feature of the context within which land values are to be ascertained – not an obligation whose delivery is dependent on maintaining land values.

16. The Local Plans should be prepared from a proportionate evidence base [158] and the strategies for housing should “take full account of relevant market and economic signals”. For housing this requires a strategic housing market assessment (“SHMA”) which will assess AH need and a strategic housing land availability assessment (“SHLAA”) to establish realistic assumptions about the availability, suitability and likely economic viability of land to meet the identified need.

17. Thus, local authorities are required to set out their strategic policies to deliver the homes needed for their area and to plan positively to meet needs using the evidence base on need. This requirement to plan to meet objectively assessed needs is thus central to and intrinsic to formulation of planning policies for housing and their application. At the heart of housing planning policy is thus a requirement which has the inevitable effect of depressing land value from what it would be worth in a market unaffected by the requirement for AH to be delivered. There is nothing unusual about planning policy having this effect: (1) requirements to provide sustainable transport, on site renewable energy, social, highway or green infrastructure; or (2) policies of restraint restricting the scale, location or type of development on a given site will similarly directly impact land value – for the short reason that land is worth what it could lawfully be developed for after meeting all requirements and overcoming all constraints.

#### *The NPPF: Viability*

18. The requisite significant boost in housing and AH supply will not be achieved if development is not viable. For this reason, the NPPF focusses on consideration of viability as part of the evidence base for the local plan and in decision making.

19. Para 173 provides as follows:

***“Pursuing sustainable development requires careful attention to viability and costs in plan making and decision taking. Plans should be deliverable. Therefore, the sites and the scale of development identified in the plan should not be subject to such a***

***scale of obligations and policy burdens that their ability to be developed viably is delivered. To ensure viability, the costs of any requirements likely to be applied to development, such as requirements for affordable housing, standards, infrastructure contributions or other requirements should, when taking account of the normal costs of development and mitigation, provide competitive returns to a willing owner and willing developer to enable the development to be deliverable.”***

20. Paragraph 174 provides that:

***“Local planning authorities should set out their policy on local standards in the Local Plan, including requirements for affordable housing. They should assess the likely cumulative impacts on development in their area of all existing and proposed local standards, supplementary planning documents and policies that support the development plan, when added to nationally required standards. In order to be appropriate, the cumulative effect of these standards and policies should not put implementation of the plan at serious risk, and should facilitate development through the economic cycle.***

21. That theme also applies in decision making on applications – emphasising the role of Local Plans [186] “translating plans into high quality development on the ground” whilst ensuring delivery [204 - 5]. Plainly the Local Plan will have judged provision of AH to be necessary to make the development acceptable in planning terms, directly related to the development and fairly and reasonably related in scale to the development [204]. Paragraph 205 is the paragraph which addresses viability in the decision making (as opposed to the plan making context):

***“Where obligations are being sought... local planning authorities should take account of changes in market conditions over time, and, wherever appropriate, be sufficiently flexible to prevent planning development being stalled.”***

22. Thus flexibility on AH may be required to prevent development being stalled. Flexibility on AH is not required to inflate land values above that necessary to incentivise development.

The NPPG

23. In the light of the above framework, the NPPG (para 016) advises that “decision taking on individual applications does not normally require consideration of viability”. It is only where delivery may be compromised (NPPF205) by the scale of the planning obligations that a viability assessment may be necessary – in other words where the developer is contending that the scale of obligations and other costs on a site specific basis in then current economic conditions impedes delivery.

24. The fundamental premise is (para 016) that:

***“A site is viable if the value generated by its development exceeds the costs of developing it and also provides sufficient incentive for the land to come forward and the development to be undertaken.”***

25. Viability assessment is (generally) required to be based on generic<sup>1</sup>, current costs and values (not costs and values achieved by a particular developer or expectations as to changes in costs and values in the future). On the latter point, it is a different exercise from that which drives open market sale prices (see e.g. para E.1.14 of the RICS Guide 2012). The latter will be impacted by the views taken by the bidders of their ability to reduce costs and increase values; their view as to future movements in the market up to the point of sale and the balance of risks and potential benefits involved - factors which are not included in the NPPG.
26. Para 019 states that AH contributions “should not be sought without regard to individual scheme viability. The financial viability should be carefully considered in line with the principles in this guidance.”
27. Paragraph 023 is the crucial paragraph and addresses how land value should be assessed.

***“Central to the consideration of viability is the assessment of land or site value. Land or site value will be an important input into the assessment. The most appropriate way to assess land or site value will vary from case to case but there are common principles which should be reflected.”***

***In all cases, land or site value should***

- ***reflect policy requirements and planning obligations and, where applicable, any Community Infrastructure Levy charge;***
- ***provide a competitive return to willing developers and landowners; and***
- ***be informed by comparable, market based evidence wherever possible. Where transacted bids are significantly above the market norm, they should not be used as part of this exercise.”***

28. *Tesco v. Dundee* applies to the NPPG just as it applies to the NPPF or the development plan. Two central points are to be noted:
- a. the second paragraph sets out the “common principles” applicable whichever valuation method is used – the choice of methods thus should not affect (or undermine) the application of the relevant common principles; and
  - b. there is a stark difference between the operative word of the first and third principle – the land value should “reflect” policy requirements but only “be informed by” comparable, market based evidence.

### “Reflect”

29. “Reflect” means to “mirror” or “exactly correspond in effect to...”. The land value used in viability appraisal must, thus, do more than simply take account of affordable housing policies – the land value must reflect (namely fully and exactly assuming compliance with) the AH policies.

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<sup>1</sup> See e.g. para 021 and 022

30. The use of the term “reflect” is no accident – the term is *necessary* to ensure that the approach to land value is based on development consistent with the development plan and s.38(6). The Mayor of London’s Draft Affordable Housing and Viability SPG November 2016 (“the Mayor’s AH SPD 2016”) is correct when it states (para 3.40):

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

31. I note that this is consistent with the Secretary of State’s response to the pre-action protocol correspondence in respect of Parkhurst Road, Islington and the recent decision in Craven Park Road, Brent.

32. I do not consider that there is any lack of clarity in the NPPF or NPPG on this central issue (Question 4 of Instructions). To the extent necessary to rely on other sources, the framework provided by s.38(6) amply demonstrates the reason and logic for the “reflect” formulation

33. Any less strong formulation would inevitably undermine the development plan because it would create a circularity which would serve to drive up land values at the expense of the requirements of the development plan (as recognised in the Craven Park Road, Brent decision). A land value which did not fully reflect planning obligations if inputted as a fixed cost would inevitably (as a matter of simple logic and mathematics) mean that the development could not afford to meet all the obligations set by the development plan. This is axiomatic and is at the heart of the circularity to which the RICS Research Paper - Financial Viability Appraisal in Planning Decisions – Theory and Practice 2015 (“the 2015 RICS Paper”) and the Mayor’s AH SPD 2016 para 3.41 refers.

34. I note that the NPPG places a greater emphasis on compliance with the development plan than does the RICS Guidance – Financial Viability in Planning August 2012 (“the RICS Guide 2012”). The latter appears to have predated the NPPG and nowhere recognises the statutory primacy of the development plan. It defines site value as:

***“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”*** – para 2.3.1.

35. The phrase “has regard to” is far weaker than the requirement to “reflect” in the NPPG. A requirement to have regard to development plan requirements is a dilution of the statutory primacy of the development plan and s.38(6). Thus unless the words “disregard that which is contrary to the development plan” are construed so as to exclude AH provision below that required by the development plan, the RICS Guide 2012 does not reflect government policy or the requirements of s.38(6). An exercise based on the RICS Guide 2012 approach will therefore not be the correct exercise required for planning decision making by the NPPF and NPPG.

*“Be informed by... wherever possible”*

36. The headline point is that this is a much weaker form of words than the obligation to “reflect” – for something to “be informed by” X, that factor has to be considered and taken into account, not mirrored or replicated or precisely followed. The contrast in words used is stark, deliberate and necessary.
37. A number of further points are to be noted:
- a. the “transactions” there referred to will reflect future market expectations, hope value and developer specific factors and thus include factors beyond those which are required by the NPPG;
  - b. the requirement is subject to the caveat “wherever possible”. The extent to which comparables themselves are consistent with the first bullet will be of central significance to whether it is so “possible”; and
  - c. from the order in which the points are put and the terminology used, the third bullet has to be read as subject to the first bullet. The “market norm” referred to must therefore be the norm reflecting planning policy – and not a “norm” which has built in an expectation of reduced AH requirements. Reading it in this way is both consistent with the words used and removes the circularity referred to above.
38. Thus the comparables should themselves reflect policy requirements<sup>2</sup>. Similarly any actual price paid for the site may be a comparable if it too reflects policy requirements. But this has a further and logically inevitable consequence – the comparable will show that policy compliant AH is viable because the land value reflects and assumes its delivery.

#### The Second Bullet

39. Of course, inclusion of a land value which will not induce a landowner to develop would impact deliverability. Viability includes the need for “sufficient incentive for the land to come forward” (para 019). The “competitive return” in the second bullet is the means to secure that incentive. I return to this under Benchmark Land Value below.
40. However, at this stage, it is notable that there is no mention in para 019 or 023 second bullet of judging “competitive return” or “sufficient incentive” by reference to market value unconstrained by, or not properly reflecting AH, obligations consistent with the development plan. This is deliberate. It is no part of the logic of planning policy (and inconsistent with the basic premise of AH policy) that, to induce him to release land a landowner has to secure a market value which does not reflect the obligations planning policy imposes on the land.

#### The RICS

41. I am told that the RICS has not amended its 2012 Guide, distances itself from the 2015 Research Paper and relies on Parkhurst Road decision and not the Secretary of State’s pre-action response (see Instructions para 3.27).
42. None of the material I have seen from the RICS provides a sustainable answer to the basic criticism of the RICS Guide 2012, or any explanation, consistent with s.38(6), as to why the its approach is correct and the approach in the NPPG is wrong. The repeated reference to the

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<sup>2</sup> Of course, the valuer will need to take into account differences between the subject property and the comparables in terms of, for example, site constraints, time of transaction and market conditions at the time, the nature of the transaction and the motivations of the parties.

market is misplaced. If, as appears to be the case that the market has a misconceived understanding of the correct approach to viability and land value in a plan led world (perhaps a misunderstanding itself contributed to by the RICS guidance), that is no reason to perpetuate the misconception.

43. In any event, the NPPF/NPPG and not the RICS Guide provide the government's view as to the appropriate approach to viability in the context of AH – it is the former that it is to be followed in formulating local authority policy and by decision makers and not the latter. The RICS Guide 2012 does not have any formal status in the planning system. It did not have government or local authority representation on the Core Working Group and is not endorsed by Government. It predates the NPPG.
44. Most importantly, it does not give the necessary statutory primacy to the s.38(6) and is written purely from a valuation perspective when the issue here is inescapably one of planning policy first and valuation consequences second. No satisfactory answer has been provided to its own experts' circularity analysis (in 2015).

Conclusion on "Land Value" in Viability Appraisal and the NPPF/NPPG

45. I therefore conclude that:
  - a. national policy requires the land value for viability appraisals to "reflect" planning policy including AH requirements – so the costs in a residual appraisal would include the costs of compliance with policy and the output is a value reflecting its potential for policy compliant development: (Question 1 of the Instructions);
  - b. there is no lack of clarity in the NPPG para 023 which reflects the requirements of s.38(6) (Question 4 of the Instructions);
  - c. comparable market information can assist in that exercise to the extent that it is consistent with that approach but not otherwise (Question 2 of the Instructions);
  - d. relevant comparables should/would thus (as a matter of straightforward logic) demonstrate that policy compliant AH was viable;
  - e. viability is not concerned with market value of the land unconstrained by, or not properly reflecting, planning policy requirements and constraints including AH; and
  - f. the RICS approach to "site value" is clearly inconsistent with national policy (and s.38(6)) in the way it is worded and in the way those words have been applied (Question 5 of the Instructions) in that:
    - i. it is considering factors not included in the NPPG assessment of costs and values; and
    - ii. more importantly, does not give development plan requirements the primacy the law requires;
  - g. in terms of hierarchy (Instructions para 4.3) in planning decision making, the development plan is the primary source (s.38(6)); the NPPF and NPPG (to which reference is required to be had in plan formulation) indicates the government's policy and can be expected to be given very significant weight in decision making (see the Court of Appeal in *West Berks v. SSCLG*); the pre-action protocol response in *Parkhurst Road* sets out how the SSCLG can be expected to approach these issues in the future; and the RICS Guide 2012 has no formal status and, unless read consistently with the NPPG and s.38(6), is of doubtful utility in a development plan or decision making context. (Question 2 of Instructions). Any rewording of it would need to recognise that



the valuation exercise has to proceed from a correct understanding of the policy framework (Question 6 of my Instructions).

### **Benchmark Land Value**

46. As indicated above, for the purpose of viability appraisal, the land value should reflect all requirements and constraints in planning policy including AH. These will serve to depress what would be the open market value absent those constraints. That is an inevitable consequence of policy imposing requirements and constraints in the public interest. Properly understood in the context of s.38(6), such land value reflects its “potential for development” (RICS Guide 2012 para E1.10).
47. There may come a point when the totality of those requirements reduce the value of the land to such an extent that it fails to provide “sufficient incentive” or “a competitive return” to landowners thus prejudicing the development of the land. That would justify inclusion of a lower obligations and thus a higher land value in the viability appraisal as an exception to policy compliance – see NPPF173/174/205.
48. The real question therefore is how to judge when that point is reached so as to justify an exception to the generally required approach. This is judged by reference to the benchmark land value (“BLV”).
49. Paragraph 024 of the NPPG states (consistent with the NPPF) that:

***“A competitive return for the land owner is the price at which a reasonable land owner would be willing to sell their land for the development. The price will need to provide an incentive for the land owner to sell in comparison with the other options available. These values may include the current use value of the land or its value for realistic alternative use that complies with planning policy”.***
50. The “competitive return” providing the “incentive” over other uses requires a benchmark land value to be established as a floor to the (residual) land value for the residential scheme.
51. My Instructions note a lack of clarity (para 4.1) regarding the appropriate methodology when approaching BLV and for developers when acquiring land. The lack of clarity is, perhaps, an inevitable consequence of the wide range of situations which can arise. However, as in para 023 of the NPPG, some common principles are discernible:
  - a. the competitive return or incentive is to be considered against the other options available to the landowner;
  - b. what is a competitive return will be highly fact and circumstances specific - and will be a matter of judgement; but
  - c. it is not to be judged by what open market value unconstrained by any planning policy would be.

### **EUV+**

52. I find the logic on EUV+ in paragraphs 3.42 – 3.49 of the Mayor’s draft AH SPD compelling: (Question 8 of the Instructions).

53. There is of course a difficulty with this method - namely ascertaining the appropriate premium. There is, so far as I am aware, no objectively verifiable evidence as to what premium a landowner requires to induce development. Further, the NPPG provides no assistance on this and the Mayor's SPD does not provide an explanation for its 20 – 30% (para 3.45 second bullet) or what factors will influence where in (or below) this range the correct figure falls. There is thus a degree of uncertainty and subjectivity built into the EUV+ approach.
54. However, it seems to me that this is not dissimilar from matters of judgment which regularly arise in the valuation field. Further, the difficulty is more theoretical than real – we know from established valuation practice what “profit” a developer requires to induce them to take on the risks and effort of developing land. The landowner/developer as developer will secure that developer's profit as a percentage of GDV in the normal way. That person may require something additional as landowner. It is difficult to see why a judgment as to what that uplift will be poses any novel issues and becomes a single question - Would £x induce the landowner to incur the effort in facilitating the development (not the risk and effort of actually carrying it out which is covered by the developer's profit)? I therefore do not see any conceptual difficulty in this approach.

Alternative Uses (Question 7 of my Instructions)

55. Often developers will point to alternative use values (“AUV”) as being higher than residential with policy compliant AH in an attempt to establish that a higher BLV.
56. The NPPG recognises that this may be permissible – para 024 – “realistic alternative use”.
57. However, it is necessary to consider the context, the realism of the suggestions and the equivalent land value on a properly detailed basis.
58. The context will normally be of a housebuilder seeking planning permission for housing and arguing that the AH obligation should be reduced below the policy requirement. The land may well have been bought as a housing development site in competition with other housebuilders and a housing scheme will have been worked up and a detailed financial appraisal undertaken for a housing scheme. The context will thus tend to demonstrate that the settled intent is to develop for housing. There will (usually) be no application for an alternative use.
59. The assertion of a more profitable alternative use is easy to make but the obvious question is - if the alternative use is more profitable than a policy compliant housing scheme, why has that alternative not been pursued. Logically, the only answer can be that by reducing AH one can make the housing scheme more profitable than the alternative use. However, that necessarily requires a large number of hurdles to be overcome: (1) the alternative use would be policy compliant and would secure permission; (2) there would be no additional costs or delay in securing that permission – or those additional costs and delays are assessed; (3) the detailed alternative proposal to be costed would be acceptable (worked up to an equivalent level of detail as the housing scheme); (4) there is a real world demand for the alternative at the values assumed; (5) the true costs and values (assessed on a comparable - NPPG compliant basis – not hope value or future increase in value basis) of a properly worked up alternative yield a higher land value than the housing scheme; (6) the housebuilder as developer rather than landowner would give up the chance of his developer's profit margin on GDV and sell on to say, a hotel developer where the GDV may be significantly different;

and (7) in the real world the landowner would really develop out the alternative rather than use it as a negotiating lever to force down AH.

60. I accept that if these hurdles could be overcome the lack of a permission may not be an insuperable obstacle to use of this method but these are high hurdles. They plainly would not be met by high level alternatives, lacking details of design, costs, values, obligations, overall returns and demand. In the compulsory purchase environment, where landowners assert alternative use values should be applied, their proposals are subject to this degree of rigour and I can see no reason for a different approach in a viability situation.

61. It is for these reasons, that the Mayor's approach in paragraph 3.49 will usually be correct:

***“Generally, the Mayor will only accept the use of AUV where there is an existing implementable planning permission for that use.”***

David Forsdick QC

Landmark Chambers

22<sup>nd</sup> December 2016