
Appendix 1

Review of London Borough of Tower Hamlets Managing Development DPD Site Viability Testing Report

1. Introduction

On behalf of St George, Quod have undertaken a review of the Site Viability Testing Report prepared by BNPP in February 2011, which forms part of the evidence base for the Tower Hamlets Managing Development DPD. The BNPP report tests the viability of ten sites within the borough using a residual land valuation model and by applying general principles and assumptions to establish whether the sites can viably provide a number of community infrastructure requirements. The News International site is one of the sites which BNPP have tested, to ascertain the implications of providing a primary or secondary school on site.

It is against this background that Quod is mindful of the guidance set out in the recently published National Planning Policy Framework (NPPF). It states that “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 threatened. 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 cost of development and mitigation, provide competitive returns to a willing land owner and willing developer to enable the development to be deliverable” (paragraph 173).

This Paper considers the viability work undertaken and considers whether this comprises a robust basis to inform emerging policy and allocation of sites, specifically having regard to the viability of the News International site, in the context of the guidance provided by the NPPF. This Paper is structured:

- To provide an overview of the inputs and assumptions which underlie the appraisals in the context of the News International site; and,
- To provide a commentary on the conclusions derived from the viability work undertaken.

2. Appraisal Assumptions

The BNPP appraisals are based on a number of development assumptions. Whilst we recognise the complexity of testing the viability impact of proposed community infrastructure requirements, based on the information presently available, Quod would like to express concern that the inputs and assumptions which underlie the assessment of viability for the News International site do not accurately reflect the site specific circumstances. Examples of our concerns include the following:

- **Mix:** The Viability Study has inconsistently applied an indicative mix of units to each of the sites tested, which in the context of the News International site is heavily skewed towards larger 3 and 4 bed family sized residential homes (30% and 35% has been applied to the News International viability tests). This does not accord with the Core Strategy's (Policy SP02 5) overall target of 30% of all new housing to be suitable for families (3 bed plus) or the emerging Managing Development DPD Policy DM3 (7), which requires a more balanced mix of 35% (1bed), 35% (2 bed), 25% (3 bed) and 5% (4 bed). No design studies have been undertaken to ascertain whether the emphasis on family accommodation is feasible.
- **Gross:Net Ratio:** The Viability Study has assumed a gross to net ratio of 85%, which is considered to be very efficient and therefore risks being over representative of the scheme value for the News International site. A more reasonable ratio to apply would be 80%.
- **Costs:** The Viability Study is considered to understate a number of the assumptions relating to cost, many of which are also inconsistent with the assumptions made by BNPP in recent work carried out in the LB of Tower Hamlets, such as the Affordable Housing Viability Study (AHVS) Update Report (December 2011). For example:
 - **Construction Costs:** Whilst the Viability Study has applied RICS Build Cost Inflation Service (BCIS) base cost assumptions with a 15% uplift for the enhanced specification for market housing and a further 15% uplift for external works, the levels assumed by BNPP are considerably lower than the December 2011 viability assessment and the GLA Toolkit benchmarks. Therefore, the approach taken has been to apply the same blanket rate of £2,151 per sq m (£200 per sq ft) to all of the ten sites tested, irrespective of assumed sales value and quality of product, density, building heights, or type of construction. Furthermore, insufficient allowances have been made for demolition, site preparation, site infrastructure, abnormal costs, car parking (especially where the car parking provision is not at grade, i.e. underground/undercroft solutions are required), public realm, landscaping and other costs. It is likely that in some instances, the assumed construction costs could only represent 60% of the potential construction costs envisaged.
 - **Professional Fees:** 10% of construction costs for professional fees have been assumed, however the December 2011 AHVS report assumes 12%, mirroring the GLA Toolkit benchmark assumption.

- Planning Obligations and Community Infrastructure Levy (CIL): The Viability Study assumed a financial contribution of £4,000 per unit to cover the required planning obligations, however the December 2011 report assumes £8,000 per unit. The AHVS appears to be more closely aligned to the Council's Planning Obligations SPD (adopted January 2012). It should also be noted that the approach taken does not take into account the impact of the Mayoral CIL on development viability. Whilst the viability study has tested ten sites that range significantly in size and number of residential units assumed, the Section 106 assumptions have remained constant, thereby failing to appreciate the considerable infrastructure costs associated with larger sites over and above the normal levels due to the scale of development proposed, such as substantial contributions towards transport improvements. Furthermore, larger sites are often expected to bring forward onsite infrastructure over and above those community infrastructure requirements tested, which the Viability Study has failed to take into consideration.
 - Contingency: The viability assessment applies a construction contingency of 3%. A reasonable minimum construction contingency of 5% should be applied. It should also be noted that different components of sites may require significantly higher contingency ie. 7.5% on infrastructure works also there is no developer contingency allowance which would be reasonable to apply, particularly for larger schemes.
 - Growth: It should also be noted that no cost growth is assumed despite value growth being assumed on the residential units at 3% per annum– this is inconsistent and growth should be removed as per the December 2011 AHVS.
- Car Parking: A value of £15,000 is assumed in relation to the private car parking spaces, whilst the construction costs do not include the additional costs associated to car parking, which in high density developments, are likely to be significant.
 - Uses: There is no assumption made in relation to mixed use development – it is assumed that the sites will be redeveloped entirely for residential uses. This is unlikely in the case of the News International site, where a mix of uses is being sought.
 - Developer Return: The assumed returns are 20% profit on cost for the private market housing and 6% for the affordable housing. The BNPP AHVS recognises that these profit levels are the minimum but this is not reflected in the Viability Testing report. BNPP recognise that it may not be feasible to deliver sites on the basis of the assumed 100% debt funding but fail to reflect this in both the cost of finance and level of developer return. A blanket approach to developer return is not considered to accurately reflect the risks associated with more complex sites, such as the News International site.

- Programme: The assumptions relating to programme are unclear, for example the construction periods are not defined nor is there any reference to whether the programmes have been varied to reflect different development types, sizes and complexities. It is therefore unclear whether the viability study acknowledges the increased cost associated with larger developments and the financial implications of longer periods over which to carry construction costs, potentially significantly underestimating the development funding and borrowing costs and the development cashflow (and sales rates). The assumed sales rate is 6 per month starting 9 months after start of construction. To ensure sufficient consideration has been given to programme, further detail is required.
- Land assumptions - An EUV based approach is not considered to be appropriate for the News International site – the resulting land value is considerably less than that which is considered to be reasonable. The viability assessment has not made an assumption for stamp duty, which is also considered to be unreasonable.

3. **Revised viability assessment**

Further to the concerns raised over the inputs and assumptions that have been applied in the BNPP viability study, Quod has considered the impact of adjusting a limited number of the assumptions. Adjustments have been made to build costs, professional fees, planning obligations and contingency so there is consistency between the BNPP AHVS and the Viability Study. In addition the gross:net ratio has been adjusted to reflect 80% and a finance cost and stamp duty cost has been applied to the BNPP assumed land cost, both of which are considered appropriate adjustments for the News International Site. The impact of these limited changes, which as a minimum are considered to be necessary in the context of the News International Site, is in the order of an additional circa £63.3 million and £64.8 million of additional costs for Scenario 1 and 2 respectively, which are not presently reported in the appraisals contained in the Viability Study.

As a consequence of the limited amendments tested, the reported shortfall for the News International site is significantly understated in table 5.2.1 of the Viability Study. When adjusting the assumptions, the shortfall generated demonstrates that the News International Site has the largest funding gap when compared to the other sites tested, as demonstrated below:

Site/ Scenario	School Type	Subsidy Shortfall
Westferry – Scenario 1	Secondary	NIL- a surplus of £49.25m is generated
Westferry – Scenario 2	Primary	NIL – a surplus of £33.25m is generated
Leven – Scenario 1	Primary	£40,000
Bow	Primary	£804,000
Alisa	Primary and Secondary	£884,000
Neptune – Scenario 2	Primary	£3,800,000
Neptune – Scenario 1	Primary	£4,400,000
News International – Scenario 2	Primary	£64,790,000
News International – Scenario 1	Secondary	£63,290,000

In considering the conclusions of the appraisals, the approach that is taken, which applies a growth rate to ascertain the amount of uplift in sales values to remove the reported ‘gap,’ is considered to be very misrepresentative. It is evident that for many of the sites, whilst reporting a high % increase needed in residential sales values and a relatively low gap funding amount against the benchmark land value, there has been no consideration as to what is the best value for money solution to delivering the sites – a payment towards securing schools sites could be a better option than imposing a risk on the delivery of those sites which will make a significant contribution to wider policy objectives, such as the News International site.

Delivery of a school on the News International site could require a significant reduction in the level of affordable housing deliverable on site and impact the tenure mix for any affordable housing element.

The Viability Study has failed to appreciate the key components of any masterplan or site specific design brief for the ten sites which have been tested. Therefore, it has not considered how a school would be configured within a masterplan nor appreciated or reflected within the inputs and assumptions, the cumulative impact of a school, for example, in terms of residential density, car parking solutions, gross:net ratios, open space provision, other infrastructure requirements, scheme permeability, mixed uses, abnormal costs, demolition costs, phasing and build programme, particularly as the Viability Study has deviated from benchmark assumptions previously applied in the December 2011 AHVS .

The Viability Study has not utilised a market value for the land and has failed to apply a level of developer return commensurate to the risks and complexity of each site tested. The conclusion of any viability study must be considered in the context of the opportunity cost of providing a school on site, recognising the number of affordable housing units forgone, the impact on overall development objectives, the resulting gap funding requirement and how this could be recovered and what it represents – not just in terms of value but also in terms of a commuted sum.

4. Conclusion

The inputs and assumptions applied in the Viability Study by BNPP are not robust and are inconsistent with BNPP's own assumptions and approach adopted in other work for the LB of Tower Hamlets, such as the December 2011 Affordable Housing Viability Study. The costs associated with the News International site are significantly underestimated and, as such, are not considered to be a robust basis on which to inform the evidence base in the context of this site. As a consequence the conclusions drawn in respect of the News International site are misleading, in terms of the true scale of the funding gap compared to the other sites tested.

Against this background, in the context of the News International site, the study is not sufficiently robust to provide evidence to support the Sites and Place Making DPD, as it has failed to fully consider how the community infrastructure requirements would impact the development viability. Therefore, it is not consistent with the NPPF, which acknowledges the fundamental requirement to give careful attention to viability and costs in plan-making.