

# **For: Thanet District Council Review of Applicant Submitted Viability Position**

**Shottendane Road  
MARGATE  
CT9 5QY**

**October 2020  
(DSP20442W)**



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Appendix I – DSP version of applicant submitted appraisal

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# 1. Notes and Limitations

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

- 1.1.6. In any event we can confirm that no conflict of interests exists, nor is likely to arise given our approach and client base. This is kept under review. Our fees are all quoted in advance and agreed with clients on a fixed or capped basis, with no element whatsoever of incentive/performance related payment.

## 2. Introduction

- 2.1.1 Dixon Searle (DSP) has been commissioned by Thanet District Council (TDC) to carry out an independent review of the Financial Viability Assessment report (FVA) supplied to the Council on behalf of the applicant, Gladman Developments Ltd, by Jones Lang LaSalle (JLL). This is in relation to the proposed development at Shottendane Road, Margate, CT9 5QY.
- 2.1.2 The viability information has been supplied in support of planning application reference OL/TH/20/0847 *'the erection of up to 450 residential dwellings (including market and affordable housing), structural planting and landscaping, formal and informal public open space and children's play area, sustainable urban drainage, with vehicular access points, including associated ancillary works and operations, from Hartsdown Road, Shottendane Road and Manston Road including access'*. The application has been submitted in outline and was validated on 13 July 2020.



- 2.1.3 Policy SP20 of the adopted Local Plan for the area (2020) requires 30% affordable housing to be provided on sites of over 15 units. The Local Plan policy therefore requires 135 units of affordable housing to be provided on site.
- 2.1.4 In presenting their viability position, the applicant has supplied to the Council the aforementioned updated Financial Viability Assessment (FVA) dated June 2020, along with electronic copies of a financial appraisal carried out using Argus Developer software. Appendices to the report include:
- Appendix 1 Site Location & Development Framework Plans
  - Appendix 2 Accommodation Schedule
  - Appendix 3 BLV
  - Appendix 4 Residential Comparable Evidence
  - Appendix 5 Valuation Schedule
  - Appendix 6 BCIS Cost Summary
  - Appendix 7 Additional Cost Breakdown
  - Appendix 8 Appraisal Summary
- 2.1.5 DSP has also had sight of the Council's online planning application files.
- 2.1.6 For general background, a viable development could be regarded as the ability of a development project to meet its costs including the cost of planning obligations, while ensuring an appropriate site value (i.e. existing use value) for the landowner and a market risk adjusted return to the developer in delivering that project. The Government's Planning Practice Guidance on Viability sets out the main principles for carrying out a viability assessment. It states:
- 2.1.7 *'Viability assessment is a process of assessing whether a site is financially viable, by looking at whether the value generated by a development is more than the cost of developing it. This includes looking at the key elements of gross development value, costs, land value, landowner premium, and developer return...Any viability assessment should follow the government's recommended approach to assessing viability as set out in this National Planning Guidance and be proportionate, simple, transparent and publicly available. Improving transparency of data associated with viability assessment will, over time, improve the data available for future assessment as well as provide more*



*accountability regarding how viability informs decision making...In plan making and decision making viability helps to strike a balance between the aspirations of developers and landowners, in terms of returns against risk, and the aims of the planning system to secure maximum benefits in the public interest through the granting of planning permission'.*

- 2.1.8 Under normal circumstances, if the residual land value (RLV) created by a scheme proposal exceeds the existing use value plus a premium (referred to as a benchmark land value (BLV) in this case) then we usually have a positive viability scenario – i.e. the scheme is much more likely to proceed (on the basis that a reasonable developer profit margin is also reached).
- 2.1.9 In this case an appraisal been run to determine the residual value after allowing for a fixed profit of 17.5% on GDV (£19,522,010). The appraisal includes only 10% affordable housing, and indicates a residual value of £2,838,920 which when compared to the stated benchmark land value of £4,742,750 indicates a deficit of -£1,903,830. The 'net adjusted' profit for the project (as presented) is therefore £16,683,090 or 15.8% on GDV. The FVA concludes that the development with 10% affordable housing '*could be deemed unviable*', but that the applicant intends to bring the scheme forward '*on this basis as it balances the need for affordable housing and local infrastructure improvements*' and in the hope that the economics of the scheme will improve over the lifetime of the development.
- 2.1.10 This review does not seek to pre-determine any Council positions, but merely sets out our opinion on the submitted viability assumptions and outcomes in order to inform the Council's discussions with the applicant and its decision making. Our report deals only with viability matters, in accordance with our instructions.
- 2.1.11 Thanet District Council requires our opinion as to whether the viability figures and position put forward by the applicant are reasonable. We have therefore considered the information submitted. Following our review of the key assumptions areas, this report provides our views.
- 2.1.12 We have based our review on the submitted Financial Viability Assessment (FVA) and the premise that the viability of the scheme should be considered based on the assumption of current costs and values. We then discuss any variation in terms of any deficit (or

surplus) created from that base position by altering appraisal assumptions (where there is disagreement if any) using the financial appraisal provided by JLL.

- 2.1.13 This assessment has been carried out by Dixon Searle Partnership, a consultancy who have over 40 years combined experience in the development industry working for Local Authorities, developers, Housing Associations and in consultancy. As consultants, we have a considerable track record of assessing the viability of schemes and assessing the scope for Local Authority planning obligation requirements. This expertise includes viability-related work carried out for many Local Authorities nationwide over the last 17 years or so.
- 2.1.14 The purpose of this report is to provide our overview comments with regard to this individual scheme, on behalf of the Council - taking into account the details as presented. It will then be for the Council to consider this information in the context of the wider planning objectives in accordance with its policy positions and strategies.
- 2.1.15 In carrying out this type of review a key theme for us is to identify whether, in our opinion, any key revenue assumptions have been under-assessed (e.g. sales value estimates) or any key cost estimates (e.g. build costs, fees, etc.) over-assessed – since both of these effects can reduce the stated viability outcome.



## 3. Review of Submitted Viability Assumptions

### 3.1 Overview of Approach

3.1.1 The following commentary reviews the applicant's submitted viability assumptions as explained within the FVA.

3.1.2 Primarily the review process takes into account the fact that the collective impact of the various elements of the cost and value assumptions is of greatest importance, rather than necessarily the individual detailed inputs in isolation. We have considered those figures provided, as below, and reviewed the impact of trial changes to particular submitted assumptions.

3.1.3 This type of audit / check is carried out so that we can give the Council a feel for whether or not the result is approximately as expected – i.e. informed by a reasonable set of assumptions and appraisal approach.

3.1.4 Should there be changes to the scheme proposals this would obviously impact on the appraisal outputs.

### 3.2 Benchmark Land Value

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

3.2.2 The RICS Guidance 'Financial viability in planning'<sup>1</sup> states that:

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<sup>1</sup> RICS Professional Guidance Note – Financial viability in planning (August 2012)

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

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

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

- 3.2.3 The revisions to the Viability PPG<sup>2</sup> and the new NPPF (updated 19<sup>th</sup> February 2019 and further updated to May 2019 in other respects) now very clearly advise that land value should be based on the value of the existing use plus an appropriate level of premium or uplift to incentivise release of the land for development from its existing use. In regard to how land value should be defined for the purpose of viability assessment it states: *'To define land value for any viability assessment, a benchmark land value should be established on the basis of the existing use value (EUV) of the land, plus a premium for the landowner.'*
- 3.2.4 The guidance defines existing use value as: *'the first component of calculating benchmark land value. EUV is the value of the land in its existing use together with the right to implement any development for which there are policy compliant extant planning consents, including realistic deemed consents, but without regard to alternative uses. Existing use value is not the price paid and should disregard hope value. Existing use values will vary depending on the type of site and development types. EUV can be established in collaboration between plan makers, developers and landowners by assessing the value of the specific site or type of site using published sources of information such as agricultural or industrial land values, or if appropriate capitalised rental levels at an appropriate yield. Sources of data can include (but are not limited to): land registry records of transactions; real estate licensed software packages; real estate market reports; real estate research; estate agent websites; property auction results; valuation office agency data; public sector estate/property teams' locally held evidence.'*

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<sup>2</sup> Most recently updated 1 September 2019



3.2.5 It states that a Benchmark Land Value (BLV) should:

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

3.2.6 The guidance further states that: *'Where viability assessment is used to inform decision making under no circumstances will the price paid for land be a relevant justification for failing to accord with relevant policies in the plan.'* It goes on to state: *'Policy compliance means that the development complies fully with up to date plan policies including any policy requirements for contributions towards affordable housing requirements at the relevant levels set out in the plan. A decision maker can give appropriate weight to emerging policies. Local authorities can request data on the price paid for land (or the price expected to be paid through an option or promotion agreement).'*

3.2.7 With regard to assuming an alternative use value to determine BLV the guidance states: *'For the purpose of viability assessment alternative use value (AUV) refers to the value of land for uses other than its current permitted use, and other than other potential development that requires planning consent, technical consent or unrealistic permitted development with different associated values. AUV of the land may be informative in establishing benchmark land value. If applying alternative uses when establishing benchmark land value these should be limited to those uses which have an existing implementable permission for that use. Where there is no existing implementable permission, plan makers can set out in which circumstances alternative uses can be used. This might include if there is evidence that the alternative use would fully comply with*

*development plan policies, if it can be demonstrated that the alternative use could be implemented on the site in question, if it can be demonstrated there is market demand for that use, and if there is an explanation as to why the alternative use has not been pursued. Where AUV is used this should be supported by evidence of the costs and values of the alternative use to justify the land value. Valuation based on AUV includes the premium to the landowner. If evidence of AUV is being considered the premium to the landowner must not be double counted.'*

- 3.2.8 It is therefore clear that the only acceptable approach to defining a benchmark land value for the purposes of a viability assessment, is the EUV+; or, exceptionally, AUV.
- 3.2.9 In this case, the benchmark is based on an assessment of the EUV of the land, plus a premium representing the amount needed to incentivise development. The site is currently agricultural land, of 18.971 ha (the wider site is 19.93 ha – or 19.53 ha according to some other sources, however JLL have not included highway areas which they explain are in the ownership of Kent County Council).
- 3.2.10 The FVA refers to various strategic level viability studies which have reviewed land values, including one carried out by DSP on development in Thanet, and take the view - which we consider to be appropriate in this case - that a rate of £250,000/ha represents the minimum land value likely to incentivise release for development. In other words, EUV plus premium. JLL have applied this to the site area (less highways) of 18.971 ha, resulting in a BLV of £4,742,750.
- 3.2.11 We consider the BLV of £4,742,750 to be an appropriate assumption.

### **3.3 Acquisition Costs**

- 3.3.1 Legal fees at 0.5% of the residualised value have been applied. Agent's fees have also been included at 1.5% of the residualised value. The resulting amounts are within typical parameters.
- 3.3.2 Stamp Duty Land Tax has also been applied to the residualised value (at a rate of 4.65%). We have applied the same SDLT calculation to the residualised value in our appraisal (which due to our appraisal having a different residualised value equates to 4.84%.



### 3.4 Gross Development Value - Private Residential

3.4.1 The planning application is in outline only. The FVA appraisal is based on an illustrative accommodation schedule, and the following table sets out the market housing mix and values assumed in the appraisal.

Code	Beds	Type 1	Type 2	Type - Gladman	Garage type	Storeys	sqm	sqft	Units	Total sq ft	Market value	Eper m <sup>2</sup>	Epsf	GDV
A2	2 bed	House	Mews/Terrace	2 bed mews	-	2	63	679	80	54,320	£215,000	£3,412	£317	£17,200,000
apt	2 bed	Flat	Flat	2 bed apt	-	-	64	690	24	16,560	£175,000	£2,734	£254	£4,200,000
C	3 bed	House	Mews/Terrace	3 bed mews	-	2	89	958	95	91,010	£265,000	£2,982	£277	£25,175,000
E	3 bed	House	Detached	3 bed det	-	2	86	930	10	9,300	£280,000	£3,240	£301	£2,800,000
F	3 bed	House	Semi-detached	3 bed semi/mews	-	2	89	958	43	41,194	£270,000	£3,035	£282	£11,610,000
I	3 bed	House	Semi-detached	3 bed semi/mews	-	2.5	102	1,095	76	83,220	£275,000	£2,702	£251	£20,900,000
M	4 bed	House	Detached	4 bed detached house	Integral gara	2	112	1,210	13	15,730	£360,000	£3,208	£298	£4,680,000
AA	4 bed	House	Detached	4 bed detached house	s det garage	2	107	1,152	13	14,976	£357,500	£3,337	£310	£4,647,500
BB	4 bed	House	Detached	4 bed detached house	s det garage	2	119	1,285	5	6,425	£372,500	£3,122	£290	£1,862,500
G	4 bed	House	Detached	4 bed detached house	Integral gara	2	97	1,045	13	13,585	£345,000	£3,552	£330	£4,485,000
K	4 bed	House	Detached	4 bed detached house	s det garage	2	108	1,159	14	16,226	£357,500	£3,315	£308	£5,005,000
P	4 bed	House	Detached	4 bed detached house	s det garage	2	125	1,350	13	17,550	£377,500	£3,014	£280	£4,907,500
P1	4 bed	House	Detached	4 bed detached house	s det garage	2	125	1,341	4	5,364	£377,500	£3,035	£282	£1,510,000
R	4 bed	House	Detached	4 bed detached house	d. attached	2	130	1,399	2	2,798	£385,000	£2,960	£275	£770,000
TOTAL/AVG							89	959	405	388,258	£270,994	£3,045	£282.68	£109,752,500

3.4.2 The above values are based on an assessment of comparables in the local area which are set out in Appendix 4 of the submitted FVA, which also includes market commentary.

3.4.3 We have reviewed the submitted evidence, and have carried out our own research of property values in the area, based on Land Registry sales data, and advertised prices on property websites for both new and resale properties.

3.4.4 We note also the comparables provided in the FVA, which include examples of recent new build sales, and asking prices, and which support the submitted values.

3.4.5 Reviewing the values data, we note that detached houses locally tend to sell for higher prices than indicated in the submitted schedule – however these are mainly much larger properties than the proposed, and when looked at on a per m<sup>2</sup> basis the sales values are the same or lower than submitted. New build flats locally have sold for higher values than proposed here, however flats make up a relatively small amount of the proposed floor area; in contrast, some of the proposed values for smaller houses exceed those that have been achieved in recent months.

3.4.6 We have reviewed the developments currently being marketed locally (some of which are included in JLL's comparables) and compared these values with sold price data, as well as comparing with properties on the resale market, taking into account that new build properties are likely to achieve a 15% to 20% premium on resale values. The values

indicated broadly align with those submitted, once location and the size/type of the proposed development are taken into account.

- 3.4.7 We have tested alternative assumptions on value for the different unit types with reference to the above-mentioned data. A more cautious set of assumptions leads to an average value of £2,950/m<sup>2</sup> and a more positive view leads to an average value of £3,150/m<sup>2</sup>. We consider, therefore, that an average value of £3,045/m<sup>2</sup> applied across the development at this stage as per the submitted appraisal, being in the middle of this range, is a not unreasonable assumption and we have not adjusted the residential GDV in our base appraisal.
- 3.4.8 It is worth noting that any improvement in the sales value assumptions (compared with a level set at the point of the appraisal) would most likely be reflected in an improvement in scheme viability. Whilst the opposite could also occur (the sales values could fall relative to the assumptions made), that is the developer's (applicant's) risk and such factors need to be kept in mind in making an overall assessment of the applicant's position.
- 3.4.9 This application is in outline, and it could be some time before a reserved matters application is submitted and the development starts on site. Detailed design is yet to be agreed. Applying even a very small adjustment to the sales values equates to a large difference in the viability outcome; a change in values of only 1% affects the GDV by £1 million. Therefore, even if all other submitted assumptions are correct, a 3% increase from the assumed sales values (thus a £3 million increase in GDV) would be sufficient to move the viability position from the submitted £1.9 million deficit to a significant surplus. This is something to bear in mind if the Council agrees to a reduced affordable housing provision being fixed at this early stage in the planning process. We will return to this in our conclusions, in the context of our overall view of site viability.

### **3.5 Ground Rents**

- 3.5.1 Ground rents have not been included in the submitted appraisal, on the basis that the Government intends to legislate against the ability to charge ground rents. This argument has been put forward for well over a year now, and the legislation was first proposed in 2017 - yet so far, no legislation has been enacted. It is our view that as a viability assessment is undertaken at the current date, it should reflect the current position. In a majority of cases put to DSP, ground rental income is included in development appraisals



and indeed it is currently still charged on new developments as far as we are aware. The intention to introduce legislation is not the same as actually legislating and as such it is our view that an allowance for revenue associated with ground rents should be included, particularly where a reduced contribution affordable housing is being proposed. However, in some cases it may be appropriate to agree a contribution based on a review of the ground rental situation at the time a scheme comes forward.

3.5.2 It is unclear whether the removal of ground rents, if and when it occurs, will result in an improvement in sales values. Whilst not a principal factor in buyers' decisions to purchase, a development which is able to market the fact that ground rents are not charged might be able to use this as a selling point/incentive compared with properties on the resale market which have a ground rental charge and therefore achieve better sales rates, if not higher values.

3.5.3 We have included a value for ground rents in our appraisal, based on £270 per flat per annum and capitalised at a yield of 5%, reflecting a now view and the regime under which the scheme has been progressed, and applying a slightly higher yield than historically assumed which allows adjustment for the higher risk arising from potential legislation. Applied to the 24 proposed private flats, this adds a total of £107,493 to the GDV, and this approach is consistent with other reviews currently conducted by DSP as well as with a range of submissions that we are receiving for review. For the time being we have not applied any ground rental income to the 24 affordable flats, although under current legislation ground rents could be charged on shared ownership homes.

### 3.6 Gross Development Value – Affordable Housing

3.6.1 Affordable housing has been valued as shown in the following table, which also indicates the proposed values a proportion of the submitted market values.

TYPE	VALUE		
	Per ft <sup>2</sup>	Per m <sup>2</sup>	% of market value
Private	£ 283.00	£ 3,045	100%
AR	£ 140.00	£ 1,507	49%
SO	£ 204.00	£ 2,196	72%
<b>AVERAGE</b>	<b>£ 152.57</b>	<b>£ 1,642</b>	<b>54%</b>

3.6.2 These assumptions are within expected parameters, and we have not adjusted them in our appraisal.

### **3.7 Development Timings**

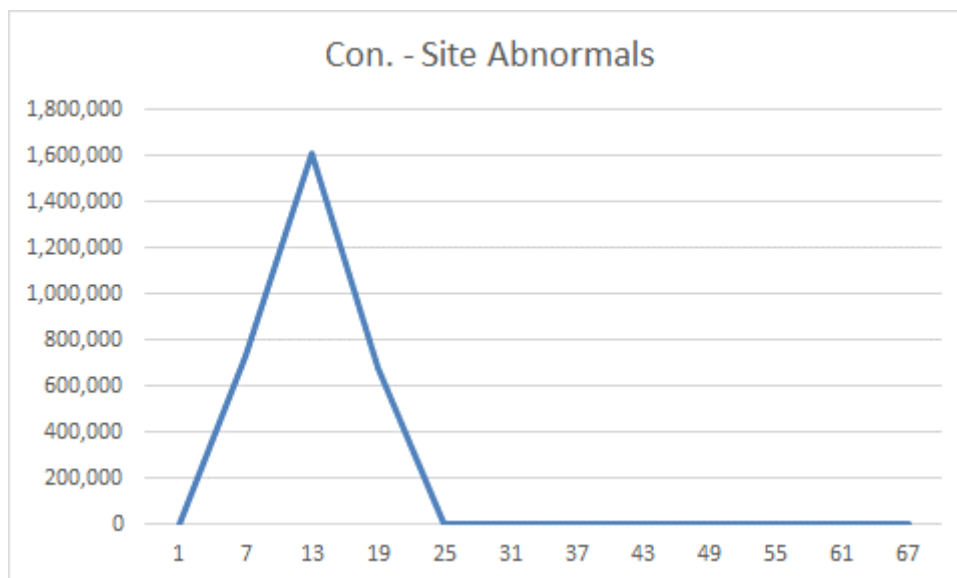
- 3.7.1 Development timings include a 6-month lead-in period, a 58-month construction period with sales beginning at month 18 and taking 50 months (a rate of 8 to 9 units per month). The FVA assumed the site will be brought forward in two sections, with each being phased (however details of phasing are to be confirmed at reserved matters stage).
- 3.7.2 Affordable housing revenue has been spread evenly throughout the construction period to model the manner in which a Housing Association would pay for the units, on the basis that affordable housing will be sold in multiple phased tranches. We consider this assumption to be not unreasonable at this outline stage and for a scheme of this size.
- 3.7.3 We note that the BCIS Duration calculator (rebased to a Thanet location factor) indicates that the site as a whole could be built more quickly – however the build rate will need to align with the site phasing and the ability of the market to absorb the units being released (with two outlets proposed which will be competing with each other). Overall, these development timings appear reasonable at this stage in our opinion.
- 3.7.4 Roughly £9 million of the £20 million submitted infrastructure/abnormal costs are included within the first 50% of the build period. The timing of the development costs within the cashflow is discussed in more detail in 3.9, below.

### **3.8 Cost Assumptions - Build Costs & Fees**

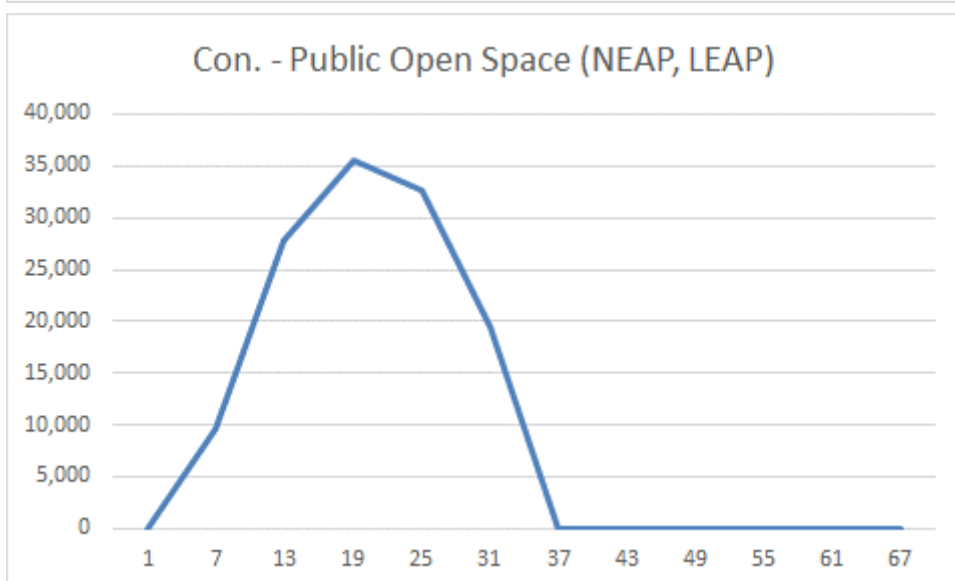
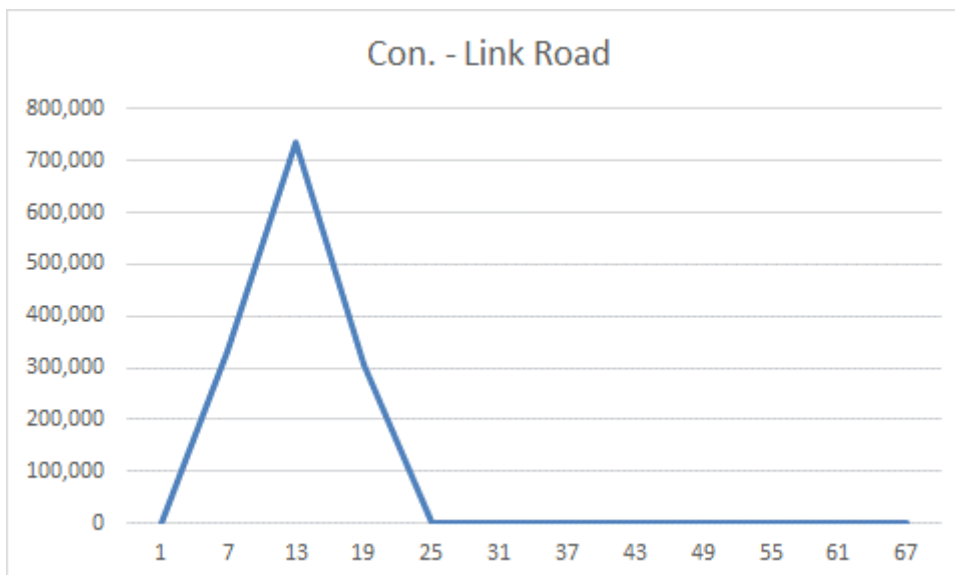
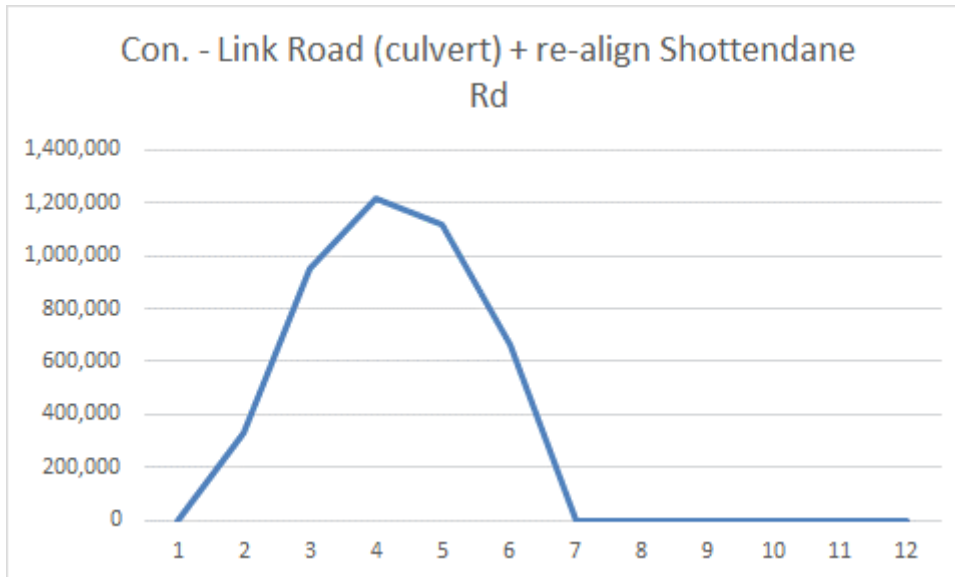
- 3.8.1 The total submitted construction cost is £76,675,715 inclusive of 5% contingency.
- 3.8.2 The submitted base build costs are stated to have been assumed at BCIS median rates rebased to a Kent location factor, resulting in an average build cost of £1,327/m<sup>2</sup> (£123.28/ft<sup>2</sup>) applied to a gross internal area of 39,270 m<sup>2</sup> (427,677 ft<sup>2</sup>).
- 3.8.3 Communal areas total 462 m<sup>2</sup> (4,973 ft<sup>2</sup>) which indicates a net:gross ratio of 87:13 for the apartments, which is within typical parameters.
- 3.8.4 Additional costs are described as follows within the FVA:

Item	Cost
Standard site works	£1,800,000
Roads and sewers	£3,850,000
Public open space	£600,000
Plot abnormalities	£2,700,000
Site abnormalities	£4,889,470
Link Road	£5,657,500
Garages	£803,500
<b>Total</b>	<b>£20,300,470</b>

- 3.8.5 Construction costs are timed via a standard S curve throughout the construction period, with the exception of the items below, with weekly timings set out in the following graphs of the 67-week project period:







- 3.8.6 Contingency has been added at 5% of works cost which is a fairly typical assumption, and appropriate in our view.
- 3.8.7 Professional fees have been included at 8% of works cost (excluding demolition) which we consider to be a not unreasonable assumption.
- 3.8.8 The submitted cost plan and the above timings have been reviewed by cost consultants ERM Surveyors, whose report is attached as Appendix 2.
- 3.8.9 ERM consider the submitted amounts for construction of the residential units, and the contingency allowance of 5%, to be a suitable assumption. They are broadly in agreement with the additional/abnormal costs; however, their analysis includes some different rates for drainage and highway infrastructure. In particular they have highlighted that they consider the lump sum inserted for "Traffic islands" to be overestimated. Overall, their estimate of gross construction cost is as follows (£3,645,000 lower than the submitted cost):

### **Construction Costs**

Residential Construction Costs	£52,724,020
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### **Additional Costs**

Standard site works	£1,800,000
Roads and sewers	£3,262,500
Public open space	£600,000
Plot abnormalities	£2,643,750
Site abnormalities	£4,889,470
Link roads	£2,829,500
Garages	£803,500
	<hr/>
	£69,552,740
<b>Contingency (5%)</b>	<b>£3,477,637</b>
	<hr/>
<b>Say</b>	<b>£73,030,377</b>

- 3.8.10 We have tested the cost estimated by ERM Surveyors in our appraisal.

### 3.9 Cost Assumptions - CIL / Planning Obligations

- 3.9.1 Thanet DC does not currently have a CIL (Community Infrastructure Levy) in place. A S106 contribution of £2,940,269 has been assumed, which is entered in the cashflow as a single payment at the start of construction. The S106 calculation has been prepared by Gladman and is set out as follows:

Item	Amount	Basis		Total
Secondary Education	£5,176.00	per	applicable house	£2,080,752.00
	£1,294.00	per	applicable flat	£62,112.00
Secondary School Land	£1,511.00	per	applicable house	£607,422.00
	£377.00	per	applicable flat	£18,096.00
Community Learning	£16.42	per	dwelling	£7,389.00
Youth	£65.50	per	dwelling	£29,475.00
Libraries	£55.45	per	dwelling	£24,952.50
Social Care	£146.88	per	dwelling	£66,096.00
Waste	£97.72	per	dwelling	£43,974.00
Health	£0.00	per	occupant	£0.00
Sports	Unknown			-
<b>TOTAL</b>				<b>£2,940,269</b>

- 3.9.2 The Council has confirmed the above figures, and has also provided updated information on planning obligations relating to Health<sup>3</sup>, for which we have included an additional cost of £388,800 in our appraisal, as instructed.
- 3.9.3 We recommend the Council verifies the assumed S106 figure, as any variation in the input amount will affect the viability outcome.

### 3.10 Cost Assumptions - Development Finance

- 3.10.1 Finance costs have been included using a rate of 6.5% including all fees.
- 3.10.2 The interest rate is the cost of funds to the scheme developer; it is applied to the net cumulative negative cash balance each month on the scheme as a whole. According to the HCA in its notes to its Development Appraisal Tool (DAT): *'The rate applied will depend on the developer, the perceived scheme risk, and the state of the financial markets. There is also a credit interest rate, which is applied should the cumulative month end balance be positive. As a developer normally has other variable borrowings (such as an overdraft), or other investment opportunities, then the value of credit balances in reducing overall*

<sup>3</sup> Based on a request from Thanet's Clinical Care Commissioning Group



*finance charges is generally the same as the debit interest charge. A zero rate of credit interest is not generally plausible and will generate significantly erroneous results in a long-term scheme.'*

3.10.3 RICS also points out that it is often the case that schemes are modelled at current costs & values i.e. ignoring inflation (as is the case here). In this case RICS Financial viability in planning Guidance Note states in appendix D 4.5 '*... current values and costs should be used together with a net of inflation finance rate. Such a net of inflation rate would be much lower than a bank rate (which naturally includes inflation expectations)*'.

3.10.4 We consider the submitted finance cost of 6.5% including all ancillary fees to be a reasonable assumption in the current market and we have not adjusted this in our appraisal.

### **3.11 Cost Assumptions - Agent's, Marketing & Legal – Private Residential**

3.11.1 3.5% of total GDV has been assumed for sales and marketing fees in the submitted appraisal. This exceeds the range typically seen, and we have reduced this to 3% in our appraisal.

3.11.2 Legal fees of £850 per unit have been applied in the submitted appraisal. This a fairly typical assumption and we have not adjusted this in our appraisal.

3.11.3 For the affordable homes, a total of £78,831 has been assumed for disposal costs. This equates to £1,752 per affordable home and is within the expected range given that the units are likely to be disposed of in phases and possibly to more than one Registered Provider.

### **3.12 Developer's Risk Reward – Profit**

3.12.1 Profit has been assumed at 17.5% of GDV for the market housing, and at 6% on cost for the affordable housing, which results in a total profit of £19,522,010, equating to a blended rate of 16.97% on the submitted GDV of £115,007,877.

3.12.2 The level of profit assumed viable is a matter of debate but in our experience through both numerous site-specific cases and strategic viability review, typically a profit on GDV of between 15% - 20% for market housing and 6% for affordable housing serves as a typical range considered acceptable to applicants; lower profit levels outside this range

are also encountered. Profit on commercial scheme elements is typically assumed to be no more than 15% on GDV.

- 3.12.3 The RICS Guidance states that: *‘When a developer’s return is adopted as the benchmark variable, a scheme should be considered viable, as long as the cost implications of planning obligations are not set at a level at which the developer’s return (after allowing for all development costs including site value) falls below that which is acceptable in the market for the risk in undertaking the development scheme. If the cost implications of the obligations erode a developer’s return below an acceptable market level for the scheme being assessed, the extent of those obligations will be deemed to make a development unviable as the developer would not proceed on that basis’.*
- 3.12.4 It goes on to state: *‘The benchmark return, which is reflected in a developer’s profit allowance, should be at a level reflective of the market at the time of the assessment being undertaken. It will include the risks attached to the specific scheme. This will include both property-specific risk, i.e. the direct development risks within the scheme being considered, and also broader market risk issues, such as the strength of the economy and occupational demand, the level of rents and capital values, the level of interest rates and availability of finance. The level of profit required will vary from scheme to scheme, given different risk profiles as well as the stage in the economic cycle. For example, a small scheme constructed over a shorter timeframe may be considered relatively less risky and therefore attract a lower profit margin, given the exit position is more certain, than a large redevelopment spanning a number of years where the outturn is considerably more uncertain. A development project will only be considered economically viable if a market risk adjusted return is met or exceeds a benchmark risk-adjusted market return’.*
- 3.12.5 Planning Practice Guidance on Viability states: *‘Potential risk is accounted for in the assumed return for developers at the plan making stage. It is the role of developers, not plan makers or decision makers, to mitigate these risks. The cost of fully complying with policy requirements should be accounted for in benchmark land value. Under no circumstances will the price paid for land be relevant justification for failing to accord with relevant policies in the plan’.* It goes on to state: *‘For the purpose of plan making an assumption of 15-20% of gross development value (GDV) may be considered a suitable return to developers in order to establish the viability of plan policies. Plan makers may choose to apply alternative figures where there is evidence to support this according to*

*the type, scale and risk profile of planned development. A lower figure may be more appropriate in consideration of delivery of affordable housing in circumstances where this guarantees an end sale at a known value and reduces risk. Alternative figures may also be appropriate for different development types<sup>4</sup>.*

- 3.12.6 The PPG, as above, although silent in terms of decision making, does set out a range of between 15% and 20% on GDV for market housing; lower for affordable housing in relation to plan making. Given that the NPPF and PPG expect planning applications to be consistent with the plan making stage, it is therefore also appropriate to assume that the range 15% - 20% on GDV (lower for affordable housing) may be considered applicable at the decision taking stage.
- 3.12.7 We consider a profit assumption of 17.5% on GDV for market housing to represent a suitable mid-point in the above range. We also consider the submitted 6% on cost for affordable housing to be a suitable assumption. We have not adjusted the profit assumptions in our appraisal.

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<sup>4</sup> <https://www.gov.uk/guidance/viability#standardised-inputs-to-viability-assessment> - Paragraph: 018 Reference ID: 10-018-20190509



## 4. Recommendations / Summary

- 4.1.1 We consider the submitted approach to assessing viability to be appropriate. We note that the application is in outline only, therefore might be subject to change at reserved matters, which could affect the viability position. As it stands, detailed information relating to many of the costs or indeed the firm scheme proposals is not available. The size of the scheme means that the viability outcome is very sensitive to relatively small looking changes in the assumptions.
- 4.1.2 The majority of the assumptions appear fair at this stage. However, there are aspects that we have queried or where a difference of opinion exists.
- 4.1.3 Reviewing the discussion above, in summary these include:
- Ground rents (see 3.5, above). We have tested the inclusion of ground rents at £270 per annum per private flat, capitalised at a yield of 4.5%.
  - Build costs (see 3.8, above). We have tested a gross build cost (including contingency) of £73,030,377, as estimated by ERM Surveyors (£3,645,000 lower than the submitted build costs).
  - S106 costs (see 3.9, above). We have added £338,000 in costs to our appraisal, based on updated information from the Council on the required planning contributions.
  - Sales/marketing (see 3.11, above). We have reduced the submitted 3.5% on GDV for sales and marketing to 3% total in our appraisal.
  - Sales values (discussed in 3.4, above). We consider the submitted values to be appropriate, however given the scheme is at outline stage we have carried out sensitivity testing on the sales values.
- 4.1.4 Applying the above adjustments to the submitted appraisal (which includes 10% affordable housing) indicates a residual value of £6,271,286 within our DSP trial version.
- 4.1.5 This residual value then has to be compared with the BLV of £4,742,750. Therefore, a surplus of £1,528,536 is indicated.

- 4.1.6 Our appraisal indicates that there is scope for a further contribution (either as on-site affordable housing, or as a financial contribution towards housing or other S106 items) in addition to the S106 contributions set out in 3.10 of this report and the 10% affordable housing proposed.
- 4.1.7 As per the submitted appraisal, we have applied a sensitivity test looking at the effect of an increase or decrease in sales values and build costs. The results are as follows:

<b>Sensitivity testing - (surplus in £ after BLV taken into account)</b>					
	<b>Construction: Rate /ft<sup>2</sup></b>				
	<b>-28.00 /ft<sup>2</sup></b>	<b>-14.00 /ft<sup>2</sup></b>	<b>0.00 /ft<sup>2</sup></b>	<b>14.00 /ft<sup>2</sup></b>	<b>28.00 /ft<sup>2</sup></b>
<b>Sales: Rate /ft<sup>2</sup></b>	<b>95.28 /ft<sup>2</sup></b>	<b>109.28 /ft<sup>2</sup></b>	<b>123.28 /ft<sup>2</sup></b>	<b>137.28 /ft<sup>2</sup></b>	<b>151.28 /ft<sup>2</sup></b>
<b>-5.000%</b>	7,748,060	2,539,825	-2,670,736	-8,224,511	-14,113,883
<b>-2.500%</b>	9,845,307	4,638,298	-570,000	-5,900,171	-11,716,682
<b>0.000%</b>	11,941,712	6,735,659	<b>1,528,536</b>	-3,680,058	-9,347,463
<b>2.500%</b>	14,036,934	8,832,063	3,626,010	-1,581,227	-7,014,944
<b>5.000%</b>	16,131,433	10,927,243	5,722,415	516,361	-4,698,465

- 4.1.8 The outcome of the appraisal is highly sensitive to relatively small changes in either build cost or sales value. Looking at sales values alone, a decrease of 5% from the estimated values would result in a viability deficit of -£2,670,736, which if deducted from the profit allowance would result in an overall profit of just under 15% on GDV (at the lower end of the range suggested in the NPPF and PPG). However, an increase of 5% from the estimated values would result in an increased surplus of £5,722,415 and therefore an overall profit position of close to 22% on GDV, exceeding the suggested range. Therefore, depending on what level of affordable housing provision and S106 contributions are agreed at this stage, the Council may wish to consider whether it would be suitable to put a review mechanism in place.
- 4.1.9 In addition, Paragraph 64 of the revised NPPF and recent Appeal precedent indicates that major developments (i.e. of 10+ dwellings) are expected to provide at least 10% of the proposed homes as 'affordable home ownership' units. The Council may wish to consider the implications for this scheme / application. As proposed, 10% affordable housing is proposed, as per the Council's desired mix of 80% of the affordable housing being for rent, therefore only 2% of the scheme is proposed to be affordable home ownership.

- 4.1.10 We need to be clear our review is based on current day costs and values assumptions as described within our review based on the current scheme as submitted. A different scheme may of course be more or less viable – we are only able to review the information provided.
- 4.1.11 No viability appraisal or review can accurately reflect costs and values until a scheme is built and sold - this is the nature of the viability review process. In this sense, the applicant and their agents are in a similar position to us in estimating positions – it is not an exact science by any means, and we find that opinions will usually vary.
- 4.1.12 As regards the wider context including the economic situation, in accordance with the relevant viability guidance our review is based on current day costs and values – a current view is appropriate for this purpose. Whilst in the short term we may with more time see evidence of negative impacts on viability, it is also possible that we may see some balance for example in terms of development cost levels, Government interventions or other factors. As set out in the PPG, a balanced assessment of viability should consider the returns against risk for the developer and also the aims of the planning system to secure maximum benefits in the public interest through the granting of planning permission. DSP will continue to monitor the established appropriate information sources. To assist the Council in its decision-making in this context, where appropriate we have considered the sensitivity of the viability position to variations in key inputs.
- 4.1.13 DSP will be happy to advise further as required.

**Review report ends**  
**October 2020**



**Appendix I – DSP appraisal summary (DSPv001)**  
**Appendix 2 – Cost plan review by ERM Surveyors**