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Financial Viability Appraisal

Regarding the development at:

Millbeck House, Oakdale Road, Arnold, NG5 8BX

27th February 2020

[redacted]

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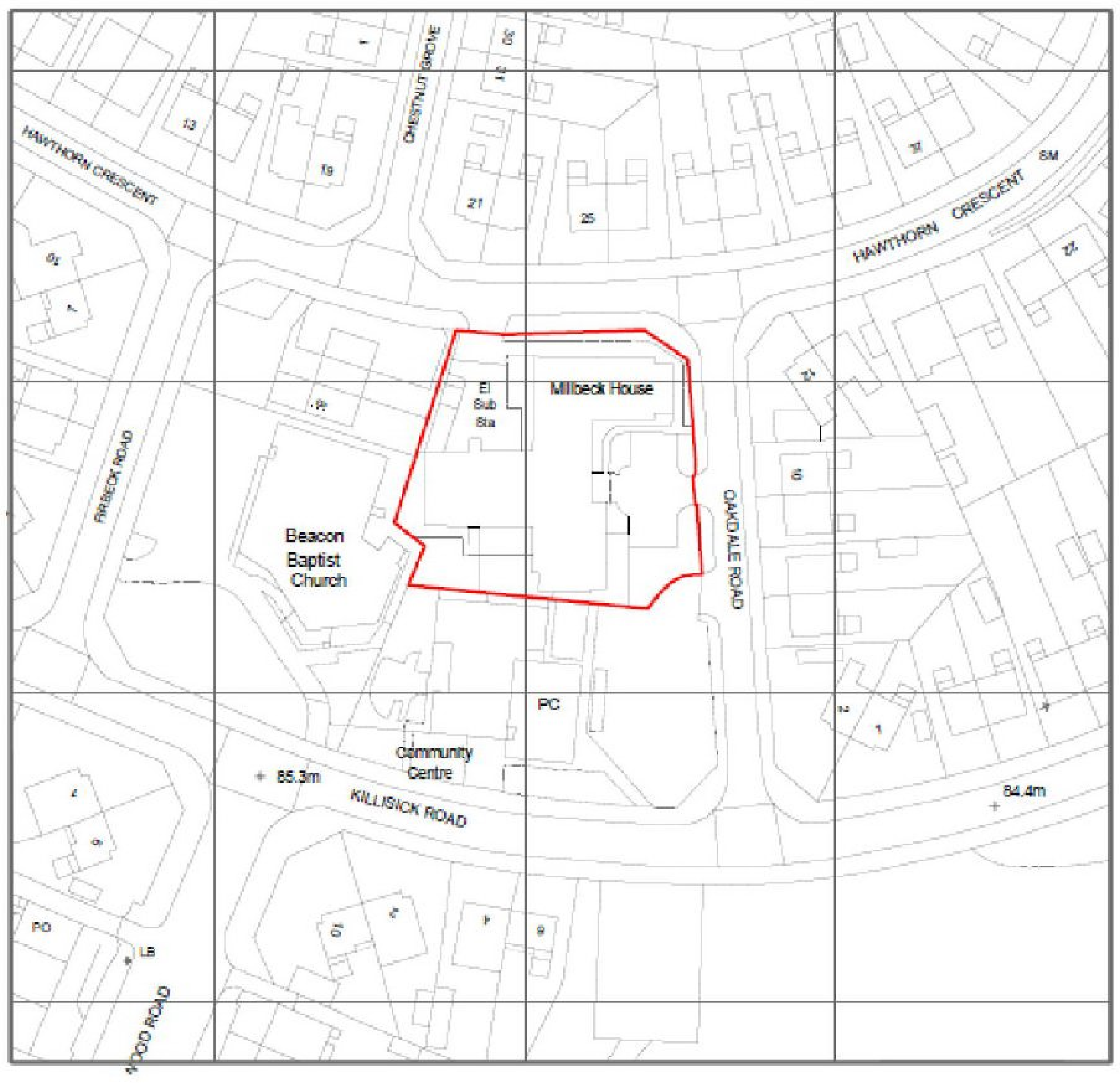
Introduction

S106 Management is instructed by Hockley Developments (Oakdale Road) Ltd to produce a Financial Viability Appraisal (FVA) to determine the level of Affordable Housing contribution that should be expected from a proposed development at Millbeck House, Oakdale Road, Arnold, NG5 8BX.

The site currently accommodates Millbeck House, a former care home (use C2) with a GIA of 1,281m2. The development comprises the conversion of the existing building to create 23 residential apartments being; 6 x 2-bed and 17 x 1-bed, along with 16 x car parking spaces, bin storage areas, cycle store and areas of landscaping. In total the development will provide 1,062m2 of residential accommodation.

Gedling Borough Council seeks an Affordable Housing contribution in accordance with Policy LPD 36 (adopted July 2018).

Location Plan



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Planning Policy

By virtue of section 38 (6) of the 'Planning and Compulsory Purchase Act', planning applications must be determined in accordance with the adopted plan of the Local Authority, unless material considerations indicate otherwise.

Therefore, our starting point is LPD 36 of the Gedling Borough Council Local Plan (adopted July 2018):

Policy LPD 36 - Affordable Housing

Planning permission will be granted for new residential development on sites of 15 dwellings or more subject to the provision of affordable housing depending on the location of the sub-market, as identified on the plan attached at Appendix C. The following percentage targets will be sought in the sub-market through negotiation:

a. Colwick / Netherfield: 10%
b. Newstead: 10%
c. Arnold / Bestwood: 20%
d. Calverton: 20%
e. Carlton: 20%
f. Arnold / Mapperley: 30%
g. Bestwood St Albans: 30%
h. Gedling Rural North: 30%
i. Gedling Rural South: 30%

In other areas, the appropriate percentage will be determined having regard to the affordable housing requirement for adjacent sub-markets and evidence of viability.

LPD 36 suggests that developments of 15 units or more in area C (Arnold / Bestwood) should provide 20% onsite Affordable Housing, thus, 4.6 units.

Further advice is provided by the 'Gedling Borough Council CIL Viability Study' (December 2014) (hereafter referred to as the CIL Study) and detail from that document is used where possible to corroborate the assumptions set out later in our report.

National Guidance is a material consideration; therefore, we also consider the 'National Planning Policy Framework' (NPPF) (Feb 2019), and the 'National Planning Guidance for Viability' (NPGV) (May 2019).

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National Guidance

National guidance on the delivery of Affordable Housing is provided by the NPPF, which replaced the previous advice in PPS3.

Paragraph 57 of the NPPF is of relevance:

> 57. Where up-to-date policies have set out the contributions expected from development, planning applications that comply with them should be assumed to be viable. It is up to the applicant to demonstrate whether particular circumstances justify the need for a viability assessment at the application stage. The weight to be given to a viability assessment is a matter for the decision maker, having regard to all the circumstances in the case, including whether the plan and the viability evidence underpinning it is up to date, and any change in site circumstances since the plan was brought into force. All viability assessments, including any undertaken at the plan-making stage, should reflect the recommended approach in national planning guidance, including standardised inputs, and should be made publicly available.

The recommended approach referred to above is set out in the NPGV (https://www.gov.uk/guidance/viability). Our report has been written in accordance with the principles set out in both the NPPF, and the NPGV.

The standard approach to viability is explained at para. 10 of the NPGV:

> ***'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.'***

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Viability

The relevance of viability is accepted in Policy LPD 36 **para 11.2.6** which states:

> 11.2.6 It is acknowledged that in some cases, the provision of the 10%, 20% or 30% of the dwellings provided for affordable housing may make the development unviable. Where this is the case, the Supplementary Planning Document confirms that a lower requirement may be justified provided there is sufficient evidence which takes account of all potential contributions from grant funding sources and a viability assessment has been undertaken by the Council which demonstrates this. Where the developer is disputing the methodology of the viability study, they must provide a full financial appraisal of the scheme and allow the appraisal to be verified, at their expense, by an independent agent chosen by the Council.

This policy statement should be seen in the context of the NPPF, and indeed subsequent Government guidance.

The concept of viability is well expressed by the NPGV, in particular para 12 which sets out the costs which should be included in any viability statement, and paras 13-17 which seek to ensure that the landowner should receive the Existing Use Value (EUV) of the site plus a premium, thus providing an incentive to the landowner to bring the site forward for development.

There are several proprietary spreadsheets in use to justify viability. We use the Housing Corporation Economic Appraisal Tool (HCEAT), developed by GVA Grimley in partnership with the Housing Corporation (now HCA); it is one of the Toolkits commonly used when considering development viability.

Our report and its conclusions are based on the application of this tool.

The next section sets out the assumptions that have been made in the preparation of the HCEAT spreadsheet examining the viability of this site; the spreadsheet is shown in **Schedule 1** of this report. The comments below address the inputs to the spreadsheet sequentially and an electronic copy can be provided to the LPA on request.

[redacted]

Spreadsheet Inputs

Proposed Residential Development (input sheet 1)

The development is summarised by the following table (plans are shown at **Schedule 2** to this report):

Unit	Area m2
1	52
2	57
3	60
4	42
5	40
6	42
7	59
8	41
9	43
10	42
11	45
12	40
13	52
14	57
15	60
16	44
17	44
18	41
19	39
20	39

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Unit	Area m2
21	40
22	40
23	43
Total	**1,062**

Affordable Housing Values (input sheet 2)

We approach this issue by firstly modelling a scheme with no Affordable Housing; if the Residual Value of this model exceeds the Benchmark Value of the site (as described below) then we produce further modelling to illustrate the maximum level of Affordable Housing that can viably be delivered by the development.

Open Market Housing Values (input sheet 2)

The Zoopla data for the NG5 Postcode is set out below:

Property type	Avg. current value	Avg. £ per sq ft.	Avg. # beds	Avg. £ paid (last 12m)
Detached	**£278,629**	£213	3.5	£271,353
Semi-detached	**£169,349**	£181	3.0	£165,895
Terraced	**£141,748**	£170	2.7	£143,497
Flats	**£118,857**	£195	1.7	£104,490

The Zoopla data suggests that the flats would achieve in the region of £2,098/m2.

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We have compared this data to relevant 'sold' transactions extrapolated from Rightmove (see **Schedule 3**) which occurred in the last 2 years, within ½ mile of our client's proposed scheme:

Address	Type	Sale Date	Area m2	£/m2	Price
8a Beechwood Road, Arnold, Nottingham, Nottinghamshire NG5 8BA	2 bed maisonette, drive & garage, rear garden	29.11.2019	93.8	£959.49	£90,000
6, Wainfleet Court, Calverton Road, Arnold, Nottingham, Nottinghamshire NG5 8GG	Top-floor maisonette	21.03.2019	60	£1,750.00	£105,000
38a Calverton Road, Arnold, Nottingham, Nottinghamshire NG5 8FN	2 bed, first-floor flat, single garage & parking spaces, private decking area	20.12.2018	46	£1,891.30	£87,000
34a Smithy Crescent, Arnold, Nottingham, Nottinghamshire NG5 7FT	2 bed maisonette, rear garden	23.11.2018	68	£1,323.53	£90,000
30 Smithy Crescent, Arnold, Nottingham, Nottinghamshire NG5 7FT	2 bed, ground-floor flat	25.09.2018	68	£1,397.06	£95,000
38d Calverton Road, Arnold, Nottingham, Nottinghamshire NG5 8FN	2 bed flat, garage & parking, garden	24.08.2018	43.7	£1,601.83	£70,000
5, Runswick Court, Arnold, Nottingham, Nottinghamshire NG5 7GW	Ground-floor maisonette	03.08.2018	54	£1,777.78	£96,000
62 Smithy Crescent, Arnold, Nottingham, Nottinghamshire NG5 7FT	1 bed ground-floor flat, in need of modernisation, front & rear garden	21.05.2018	43.8	£1,528.54	£66,950
18a Smithy Crescent, Arnold, Nottingham, Nottinghamshire NG5 7FT	2 bed maisonette, single garage & parking, rear garden	04.05.2018	67	£1,567.16	£105,000
			Avg. £/m2	**£1,478.87**	

The average £/m2 value from Rightmove is lower than that taken from Zoopla, this is because it focuses on transactions from the immediate area surrounding the development, rather than Zoopla which encompasses the entire NG5 postcode.

There is also evidence of the often-seen inverse correlation between £/m2 values and unit area meaning that we would expect the smaller flats to achieve higher £/m2 values than the larger.

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In addition to examining the 'sold' data above, we have also looked at flats currently for sale in the surrounding area located within 1 mile of the subject site:

Address	Type	Sale Date	Area m2	£/m2	Price
Kingswell Avenue, Arnold, Nottinghamshire, NG5 6SY	2 bed ground floor flat, allocated parking	for sale	63	£1,984.13	£125,000
Kingswell Avenue, Arnold, Nottingham	2 bed ground floor flat, gated allocated parking	for sale	58	£2,068.97	£120,000
Larkspur Avenue, Nottingham	2 bed maisonette, private rear garden, garage	for sale	51	£2,254.90	£115,000
73 Kilnbrook Avenue Arnold, Nottingham, NG5 8DA	1 bed, modern first-floor flat, allocated parking	for sale	63	£1,746.03	£110,000
Galway Road, Arnold, Nottinghamshire, NG5 7AY	2 bed ground floor maison-ette, driveway & garage	for sale guide price	55	£2,000.00	£110,000
Furlong Court, Furlong Street, Nottingham	2 bed, second-floor flat, allocated parking	for sale	46	£2,282.61	£105,000
Edison Way, Arnold, Nottingham	2 bed, modern ground-floor flat, off-street parking	for sale guide price	54.7	£1,828.15	£100,000
Chelsbury Court, Arnold	1 bed, top-floor flat, single garage	for sale fixed price	48	£1,770.83	£85,000
Coppice Road, Arnold, Nottingham, Notting-hamshire, NG5	2 bed flat	for sale	57	£1,228.07	£70,000
			Avg. £/m2	**£1,896.31**	

The average for sale price is higher than that of the recent sold transactions on Rightmove, however, given current market stagnation, it is reasonable to suggest that asking prices may not necessarily be achieved.

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We have proposed a value of £100,000 for the smallest flat, to produce a £/m2 cost of £2,564 and adjusted the remaining values to match the inverse correlation referred to previously, as follows:

Unit	Area	£/m2 value	Price
1	52	£2,308	£120,000
2	57	£2,228	£127,000
3	60	£2,333	£140,000
4	42	£2,548	£107,000
5	40	£2,550	£102,000
6	42	£2,548	£107,000
7	59	£2,288	£135,000
8	41	£2,561	£105,000
9	43	£2,558	£110,000
10	42	£2,548	£107,000
11	45	£2,533	£114,000
12	40	£2,550	£102,000
13	52	£2,308	£120,000
14	57	£2,228	£127,000
15	60	£2,333	£140,000
16	44	£2,545	£112,000
17	44	£2,545	£112,000
18	41	£2,561	£105,000
19	39	£2,564	£100,000
20	39	£2,564	£100,000
21	40	£2,550	£102,000
22	40	£2,550	£102,000
23	43	£2,558	£110,000
Total	**1,062**	**£2,453.86**	**£2,606,000**

For clarity, we have run the appraisal with the average £/m2 value, which is £2,453.86

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In addition to the sales values we have included a lump sum of £115,000 to allow for the freehold ground rent; this is based upon passing rents of £300pa and applying a yield at 6%.

Timing (input sheet 2)

This FVA is to be read in conjunction with a detailed planning application which we expect to be granted within 3 months. There will be a 3-month period following this to produce building regs. drawings and obtain all fixed price quotations.

Construction is projected over an 18-month period with sales expected between months 16 and 22.

The 6-month period before commencement of build has not been included in our calculations.

Construction Costs (input sheet 2)

We refer to the BCIS data, as shown below:

£/m2 study

Description: Rate per m2 gross internal floor area for the building Cost including prelims.
Last updated: 01-Feb-2020 00:47

Maximum age of results: Default period

Building function (Maximum age of projects)	£/m² gross internal floor area						Sample
	Mean	Lowest	Lower quartiles	Median	Upper quartiles	Highest	
Rehabilitation/Conversion							
816. Flats (apartments)							
Generally (15)	1,577	470	973	1,249	1,613	5,464	84
1-2 storey (15)	1,943	538	1,033	1,300	2,228	5,464	20
3-5 storey (15)	1,337	470	997	1,197	1,429	5,055	48
6 storey or above (15)	1,906	527	1,046	1,481	2,508	4,580	15

[redacted]

[redacted]

The HCEAT appraisal has been run with the lower quartile £/m2 cost for rehabilitation / conversion of £1,033. The area of the flats (1,602m2), represents 90% of the building, with all other areas allowing for communal spaces; the HCEAT Spreadsheet has been run with a corresponding correction factor.

The BCIS data only allows for the costs of creating the envelope of the proposed dwellings, all external and abnormal work is addressed subsequently in our analysis.

Fees (input sheet 2)

10% for fees is the default value of the HCEAT Spreadsheet and is the commonly accepted industry standard allowance.

Contingency (input sheet 2)

5% for contingencies is the default value of the HCEAT Spreadsheet and is the commonly accepted industry standard allowance.

Section 106 Payments (input sheet 2)

Gedling BC charge CIL per zone, Millbeck House is located in Zone 1 where no charge currently applies for residential development. Therefore, no allowance has been made in our calculations.

CIL Rate

The rate at which CIL will be charged shall be:

Development Type			
Residential	Zone 1 £0/sqm	Zone 2 £45/sqm	Zone 3 £70/sqm
Commercial	Borough wide		
Retail A1, A2, A3, A4, A5	£60/sqm		
All other uses	£0/sqm		

[redacted]

[redacted]

Abnormal Development Costs (input sheet 2)

As mentioned previously, the BCIS data only allows for the costs of constructing the envelope of the proposed dwellings; external and abnormal costs are summarised by the table below:

Abnormal Work Required	Quantity	Cost per Unit	Total Cost
Site preparations	1	£25,000	£25,000
Services	23	£2,000	£46,000
NHBC or similar	23	£2,000	£46,000
Hard landscaping	305	£80	£24,400
Soft landscaping	200	£30	£6,000
Total			**£147,400**

The HCEAT has been run with the corresponding figure, under the heading ‘Site Abnormals.’

Site Acquisition Costs (input sheet 2)

The EUV of the site, as explained subsequently in our reporting, is £770,000; we have included acquisition costs of £30,000 which incorporates £28,500 in SDLT.

Finance Costs (input sheet 2)

Typically, banks are prepared to lend only the building cost (£1.36m) of this type of development; their arrangement fee will be 2% and the spreadsheet carries an input of £27,000.

While base rates are at a historic low level, cost of funding expressed as a percentage above LIBOR is at historically high figures, therefore an interest figure of 7% is used in the spreadsheet.

[redacted]

The spreadsheet includes misc. lending fees of £10,000; made up from the bank surveyor's initial valuation fee of £5,000, monitoring fees while the project progresses of £2,500, and £2,500 in other bank fees.

Marketing Costs (input sheet 2)

The HCEAT spreadsheet has default values of 6% for marketing and £600 per unit for legal fees; as a compromise, we have adopted a marketing cost of 3% and legal fees of £1,000 per unit.

Developer Profit (input sheet 2)

The NPGV contains the following advice at paragraph 18:

> ***How should a return to developers be defined for the purpose of viability assessment?***
>
> *'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 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.*
>
> *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.'*

Paragraph 008 of the NPGV provides further guidance:

> ***'How should a viability assessment be treated in decision making?***
>
> ***Where a viability assessment is submitted to accompany a planning application this should be based upon and refer back to the viability assessment that informed the plan; and the applicant should provide evidence of what has changed since then.'***

[redacted]

We have referred to the Gedling BC CIL Viability Assessment, produced by the council in December 2014, which, at Para. 7.5 identifies a developer profit of 20% of GDV; the HCEAT appraisal has been run accordingly.

> 7.5 Developer's Profit
>
> Developer's profit is generally a fixed percentage return on gross development value or return on the costs of development to reflect the developer's risk. In current market conditions and based on the minimum lending conditions of the financial institutions, a 20% return on GDV is used for the residential viability appraisals to reflect speculative risk. A 17.5% return is applied to the commercial development in recognition that most development will be pre-let or pre-sold attracting a reduced level of risk.

[redacted]

[redacted]

Benchmark Value

The NPGV provides a standard methodology for determining Benchmark Land Value (BLV).

Paragraph 15 requires that the EUV of the site should be identified:

> *'Existing use value (EUV) is the first component of calculating benchmark land value. EUV is the value of the land in its existing use. 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 (excluding any hope value for development).*
>
> *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.'*

We have sought advice from John Carter MRICS to determine an EUV of the site:

> 'The following is my assessment regarding a Benchmark valuation for a premises known as Millbeck House, Oakdale Road, Arnold, Nottingham, NG5 8BX.
>
> The property comprises a modern, purpose-built Care Home premises having accommodation extending to 32 single bedrooms with additional brick wall construction beneath the concrete tiled floor.
>
> The property was purchased unconditionally very recently following an Open-Market sales exercise.
>
> The selling agents; Innes England, have confirmed to me that the property was openly marketed based on unconditional offers and that considerable interest was generated during this process. The eventual purchase was made in the face of competition from several under-bidders, and the property was purchased at a sum of £770,000
>
> It is my opinion therefore, that an appropriate Benchmark value for this property reflects the sale price following an arm's-length open-market sales exercise and is at the sum of £770,000.'

[redacted]

[redacted]

Paragraph 16 requires that a premium should be added to the EUV (EUV+) to incentivise the landowner to bring the site forward for development:

'The premium (or the 'plus' in EUV+) is the second component of benchmark land value. It is the amount above existing use value (EUV) that goes to the landowner. The premium should provide a reasonable incentive for a landowner to bring forward land for development while allowing a sufficient contribution to fully comply with policy requirements.

Plan makers should establish a reasonable premium to the landowner for the purpose of assessing the viability of their plan. This will be an iterative process informed by professional judgement and must be based upon the best available evidence informed by cross sector collaboration. ***Market evidence can include benchmark land values from other viability assessments.*** *Land transactions can be used but only as a cross check to the other evidence. Any data used should reasonably identify any adjustments necessary to reflect the cost of policy compliance (including for affordable housing), or differences in the quality of land, site scale, market performance of different building use types and reasonable expectations of local landowners. 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).'*

The EUV of site as explained above is £770,000, this is inclusive of a landowner premium in accordance with the RICS guidance.

Paragraph 17 allows the BLV to be determined by an alternative Use Value (AUV):

'For the purpose of viability assessment alternative use value (AUV) refers to the value of land for uses other than its existing use. 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 would fully comply with up to date development plan policies, including any policy requirements for contributions towards affordable housing at the relevant levels set out in the plan. Where it is assumed that an existing use will be refurbished or redeveloped this will be considered as an AUV when establishing BLV.

(Continued on the next page)

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[redacted]

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 up to date 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.'

In this case it is not appropriate to consider the AUV of the site.

The standard approach to viability is to compare the BLV of the development site with the Residual Value calculated by the (HCEAT) viability spreadsheet. It is only if the Residual Value of the development exceeds the Market Value (Benchmark), that it will be viable for a contribution to be made towards Affordable Housing.

[redacted]

[redacted]

HCEAT Spreadsheet Conclusions (spreadsheet summary)

The full spreadsheet appears at **Schedule 1**, and the key conclusions are set out in the summary section. They are also repeated for convenience below:

Sales	**£2,721,000**
Less Costs	
Construction Costs	£1,218,940
Other SIte Costs	£366,336
Marketing	£105,630
Finance Costs	£168,979
Developer Profit	£544,200
Residual Site Value	**£316,916**

To determine the viability of the provision of Affordable Housing, the Benchmark Value of the site as stated above **(£770,000**), is deducted from the Residual Value calculated by the HCEAT spreadsheet. If the result is negative, as it is in this case (**-£453,084**), the development cannot viably provide a contribution towards Affordable Housing.

[redacted]

[redacted]

Conclusion

The following table has been compiled using data from the HCEAT spreadsheet to reveal the profit that the developers will earn from this project:

Spreadsheet Residual Value	**£316,916**
Plus Spreadsheet Developer Profit	**£544,200**
Less Benchmark Value	**£770,000**
Actual Profit	**£91,116**

This presents a return of 3.3% which is clearly significantly lower than the 20% identified previously.

Any contribution towards Affordable Housing would further reduce this level.

This report demonstrates that the scheme can be considered policy compliant without the provision of any Affordable Homes or S106 contributions towards Affordable Housing.

[redacted]