

Just Space Response to the GLA's draft response to Panel Note 9

The panel, in its Note 9, had asked the Mayor to prepare, in liaison with other participants, a short summary note identifying the main areas of dispute about the viability evidence. Rather than liaise with other participants, the Mayor chose to write its own draft and then leave it to the panel secretariat to circulate the draft to other participants and to assimilate their responses.

Comments from Just Space, submitted to the Panel Secretariat 1 May 2019 but not incorporated in the Mayor's draft or published on the Panel web site. Another version shows these comments as insertions in the GLA draft. Both are at <https://justspace.org.uk/hearings-eip-2019/> - M92

The published version of the GLA document of 8 May is at https://www.london.gov.uk/sites/default/files/nlp_ex_35a_gla_note_in_response_to_panel_note_9_-_matter_92_viability.pdf

A. List of Policies likely to have a significant effect on development costs and/or development values

1. Social and Community Infrastructure (Policies S1 to S7)

LPVS Costings for do not include allowance for **schools and health care, child care and community services, protection or re-provision of lost community assets, leisure facilities**. These are commonly included in all S106 agreements and should be priority claims on S106 and CIL contributions (yet policy Df1D wants to de-prioritise these. We object). These are the core conventional elements of planning gain contributions: "to make the development acceptable in planning terms", and are always "directly related to the development".

The funding demands are significant, although the social and community infrastructure essential to the delivery of the Mayor's Good Growth strategy does not seem to be costed.

However, London 2050 Infrastructure Plan notes £68bn capital expenditure needed for schools from 2016-2050, 5% of total infrastructure costs, with an observed £22bn funding gap (p. 70, 73).

Details of the policy cost implications are in Annex H of the LPVS Technical Report need to be more exhaustively considered – we refer the Inspector to this document to consider that many policies in the Draft New London Plan have cost implications, many related to the conventional expectations of the purpose of S106 contributions, and need to be taken into account. From the LPVS, and the GLA contribution to that note summarising what has been considered in the costs estimations for the LPVS, it is clear that these have not been adequately considered.

- The positive value of many aspects of a development

Thus, LPVS 5.8.1 notes that some policies might enhance the value of developments – we suggest a number of these would include community and social infrastructure provision eg being close to a good school, having a well maintained and valued neighbourhood park, vital and lively town centres.... These should be prioritized in S106 agreements to ensure best value creation for public good.

Many positive aspects of a development relevant to the Mayor's Good Growth policies (social and community infrastructure, green, open and amenity spaces, protection of vital and attractive meantime and existing uses) will bring value to a development. As these might traditionally be expected to be provided by a developer anyway to bring forward good design as standard, and to enhance sales or rental value and developer reputation, these should have a priority claim on S106.

2. Transport costs

The DNLP expects that developments will bear a significant proportion of transport infrastructure costs, but these are not costed in the LPVS, except as more-than-abnormal costs, where it is acknowledged that S106 cannot cover these. Thus, despite being stated as a priority for S106 funding in Policy DF1D, they are not considered in estimating the anticipated significant costs.

In terms of the relation between the LPVS and the London Plan (Table 10.1 outlines the numerous transport infrastructure projects to be funded in the plan period) this is a real elephant in the room. Table 5.2 of the LPVS addendum outlining the approach to abnormal costs makes no mention of transport costs, which are likely to be highest in the hard to develop areas where new transport infrastructure is essential to the feasibility of the development, and where policy DF1D anticipates a strong contribution (ie where viability issues are negotiated and not fast tracked).

The Mayor's transport strategy has a deep financial shortfall, and it is our assumption that TfL is anticipating accessing S106 funds (as per Table 10.1 and Policy DF1D), alongside the other strategies which include becoming a major retail and commercial developer and Build to Rent landlord – an astonishing diversification of function – Transport for London business plan, p. 114: "We will do more to leverage our position as one of London's largest landowners, developing our property, retail, advertising, telecoms and consultancy businesses to continue to deliver ongoing income streams." We note here that the Mayor will have substantial conflict of interest in planning decisions to enhance his own income streams.

DNLP: 2.1.11 "In the Mayor's Transport Strategy a number of priority infrastructure schemes have been identified that would bring significant regeneration benefits, including the potential to unlock substantial homes and jobs growth in specific Opportunity Areas. The development value in these areas can, in some cases, also contribute to the funding of the schemes." The costing for these is not given precisely, but the TfL Business Plan notes a budget need of £2bn per annum for capital investment (p. 55).

The dependence of the Mayor's transport policy on s106 monies is made clearer in Chapter 11 of the DNLP:

11.1.30: "However, most of the schemes listed in table 10.1 are currently unfunded and additional sustainable funding sources and project-specific deals and grants will be needed alongside contributions from London boroughs and the private sector."

11.1.28 Transport in London is funded through a combination of sources, including:

- Business Rate Retention under Mayoral control, which is replacing existing direct Government grants for operations and new capital investment from 2017-18
- revenue from fares and other 'user pays' sources (e.g. Congestion Charging)
- non-fare sources (e.g. advertising and property)
- contributions from the London boroughs and the private sector, for example, developer funding for associated transport investments

- other specific grants
- TfL 'prudential borrowing' against future revenue

11.1.32 The Mayor is considering options for ensuring all beneficiaries of growth contribute to it, and for sweating London's existing assets to deliver efficiency savings.

11.1.66 Through this Plan the Mayor is determined to tackle the housing crisis and support London's continued growth in a sustainable and inclusive way. This chapter has set out how the funding gap must be met if the infrastructure to support growth is to be planned and delivered at the right time. The step change in housing delivery that London needs cannot happen without it. The Mayor needs new fiscal tools to fund this infrastructure. Where it can be funded privately, he requires a supportive regulatory regime so that it can be provided when needed."

However, it is clear that this expectation is not tested or costed in the LPVS which notes that:

"14.2.9 Other policies of the plan have also been tested including accessibility and energy standards, transport, community and green infrastructure requirements and Mayoral and Borough CIL and S106. **These represent modest costs as a proportion of development value and typically have limited impact on overall viability.**"

This claim is hard to credit unless it is anticipated that S106 funds will contribute to modest and small local transport needs of developments, such as enhanced bus routes and refurbishing streets.

But imposing further transport costs has been shown to have a terrible effect on the achievements of the London plan policies: it is the transport costs of Vauxhall Nine Elms and Old Oak Park Royal which have yielded almost no social rent or LAR level housing, and very little other intermediate housing, which has needed grant contributions. On this score, 5.6.14 of the LPVS notes that "Some sites have other costs that are exceptional, reflecting the specific development found there, and which are not readily replicated for policy testing purposes – for example new transport or social infrastructure. While sites have been tested with onsite and offsite infrastructure requirements, scenarios with very substantial exceptional costs are atypical and lie outside the scope of this testing."

Yet Policy T1 of the London Plan notes that:

"A Development Plans and development proposals should support and facilitate:

...
2) the proposed transport schemes set out in Table 10.1."

Since many of these (vaguely costed) projects are in the medium to high cost category, in the region of 100s of millions, £1bn or higher, clearly there will be many schemes which will be burdened with these more than abnormal costs.

3. Affordable workspace

This has a very limited impact on overall build costs as they are a small percentage of the overall GDV (less than 1%) (LPVS 7.2.10) and they can also add value and bring vitality to early phase developments, increasing early yields in a scheme. (cf London First M92 p. 5). We oppose efforts to needlessly limit contributions to support London's vital and diverse economy – to facilitate the Mayors GG5, we oppose the policy DF1D making this a low priority.

Appendix B. Assumptions about costs of different types of development

(a) a large proportion of development explicitly falls outside the normal cost assumptions of the LPVS.

- **Abnormal costs eg Opportunity Areas, brownfield sites**

LPVS: 5.6.14 “Some sites have other costs that are exceptional, reflecting the specific development found there, and which are not readily replicated for policy testing purposes – for example new transport or social infrastructure. While sites have been tested with onsite and offsite infrastructure requirements, scenarios with very substantial exceptional costs are atypical and lie outside the scope of this testing. Such schemes may be subject to site specific testing where the infrastructure cost is preventing delivery. It is also noted that, where there are exceptional development circumstances and associated costs, these may enhance market values and/or increase costs and it would be expected that these would be reflected in the land value for the site.”

We note that this applies to more than 300,000 of planned homes.

From the Mayor’s “Homes for Londoners: Affordable Housing and Viability SPG”:

“2.8.0. Opportunity Areas and Housing Zones are key sources of housing supply in London. They are, by their nature, complex to bring forward and often require significant investment in infrastructure. They are also of a scale that can create fundamentally new places and communities. Significant research and an in-depth understanding of the area, its strengths and weaknesses, and how to deliver a successful place underpin the development of an Opportunity Area Planning Framework.” (p. 31).

At LPVS 5.6.13, sensitivity testing includes consideration of abnormal development costs. In these scenarios, fewer of the land value bands were viable, and to be viable intermediate rather than social rent products were required. Grant contributions were also required.

However, 5.6.14 makes clear that large transport costs, as per DNLP Table 10.1 are considered outside of these “abnormal” costs.

- **Very tall buildings**

The LPVS has not tested the cost implications of very tall buildings at the kinds of densities the mayor is currently supporting and approving (say, 40 stories with 600dph).

Although the claim is made that this has been the focus of the LPVS, we do not find any distinction between very high buildings and “21+ stories” which is below the threshold at which development costs significantly increase (say 25 stories) and where as a result affordable housing is hard to deliver – top stories are usually high end homes. These heights are currently being delivered even in some well-located suburban areas. The NLA Tall Buildings Survey (2018) shows average heights of tall buildings in the pipeline at 29 stories, with more than a third of buildings above 30 stories. As the Mayor defines tall buildings as above 30m (about 10 stories) the policy and cost implications of anticipated and actual delivery have not been costed.

LPVS 14.1.5 We have identified and provided indicative costs of those policies which might be expected to impact on development viability and therefore provide a thorough review of

the impact on development viability of the draft London Plan. Important in this respect are the policies for delivery of affordable housing, carbon reduction standards, housing accessibility, standards for cycle provision and mixed-use schemes. Overlaying these specific policies is the need to make best use of development land that is available and therefore the testing undertaken has focused on higher density schemes and taller buildings although not exclusively.

LPVS 7.2.4. Commenting on office building cost structures, the LPVS notes that economies of scale only come in above 40 stories, based on Frank Knight tall Building report.

Appendix C. Assumptions about values of different types of development

Affordable Housing Values:

These figures are too high, and do not reflect the social rent levels which need to be achieved. Data here from London Tennant’s Federation sheet (submitted for inclusion in EIP Library).

Social Rent:

Average weekly rents and service charges:

Council £106 + £9 (2017/18)

Housing Association £122 (2018) + £11

Weekly London Affordable Rents are set out below. A 2017/18 3-bed London Affordable Rent is just less than 50% market rent.¹ It is 52% higher than the average 2017/18 council rent and 32% higher than the average 2018 housing association rents. Service charges are extra.

	2017/18	2018/19	2019/20
Bedsit & one beds	£144.26	£150.03	£155.13
Two beds	£152.73	£158.84	£164.24
Three beds	£161.22	£167.67	£173.37
Four beds	£169.70	£176.49	£182.49
Five beds	£178.18	£185.31	£191.61
Six or more beds	£186.66	£194.13	£200.73

Appendix D: Main benchmark land value related assumptions in viability evidence documents and alternative figures suggested by participants

(a) How profit is dealt with – more can be asked for from developers

We are concerned that profit expectations are set too high, and oppose any attempts to raise these norms – and oppose 20% as the highest, this exceeds industry norms and expectations internationally, as well as recorded achievements which according to LPVS Annex G Chart G only sometimes achieve 15%, and for most years, and most developers, especially for SME developers, is much lower. London First note that the NPG Para 018 sets 15-20% of GDV as possibly most appropriate. We note chart G3 in the technical addendum where average housebuilder profits range fall in this range but do not ever reach 20% with some crisis years of losses, but we also note extensive media reporting of super profits from house builders. We do not see

why the Mayor should legislate to INCREASE developer profits rather to improve achievement of public benefit through sharing in the value uplift achieved by public investments.

We are concerned that developers are not expected to absorb any risk in undertaking development. The implications of lower GDV and higher land prices are borne by loss of public benefit (a less equitable split of the profit) if the profit guarantee of 15-20% is made into policy. Further, higher GDV and lower land prices can yield windfall gains for developers. The review mechanisms proposed in the SPV go some way to managing this and need to be carefully maintained especially with any change of developer/owner through the course of the development.

However, we have noted a tendency of developers to fall back on review mechanisms as a way of resolving conflict between developers and LPAs over viability assessment outcomes. Developers claim that this is better than determining levels of affordable housing on assumptions, because the level will be based on actual returns. We have our doubts and see it as a tactic to reduce affordable housing, through control of delivery and costs etc where the viability assessment indicates more can be delivered.

We also note that the format of modelling profit affects the potential for viability. In a forthcoming paper from Henley Business School (Reading University) Real Estate Professor Pat McAllister, the format adopted by the Mayor and the LPVS of estimating EUV plus a premium (based on the anticipated development) yields a lower proportion of affordable housing and planning gain contributions than alternative measures such as “market value of land expressed as a proportion of gross development value”. This alternative format, he argues, yields a clearer relationship between returns to the landowner and returns to the developer. (This and other papers referenced here have been submitted for the EIP Library).

In addition, research (Neil Crosby, Steven Devaney & Peter Wyatt (2018) The implied internal rate of return in conventional residual valuations of development sites, *Journal of Property Research*, 35:3, 234-251) has shown that the broad brush calculation of the proportion of costs to gross development value, the model adopted to estimate developer profit in the LPVS, does not take account of the actual rates of profit earned within a project (internal rate of return - IRR) or changes over time, including length of period of development. Developments completed within a year or two can earn considerably higher IRR (up to 70%); to earn a consistent IRR some projects, especially short term build projects, perhaps such as Build to Rent developments, could withstand much higher imposition of planning gain expectations. This could mean that a large loss of planning gain might follow from the fast track approach to viability assessments. Again, a closer monitoring over time of how appropriate levels of planning gain can be achieved over the life of a project, and also a more nuanced and realistic approach to calculating returns and profit as developers and real estate investors actually do, is encouraged.

In a study undertaken by Bob Colenutt and Pete Redman for the PEACH viability model in Custom House the GLA figures for costs were used, but the real impact on viability was noted to be:

- interest rate and inflation assumptions
- the land costs
- the amount of cross subsidy from market housing to affordable housing
- development values and assumptions about annual price inflation
- developer profit
- local uplift assumptions such as Cross Rail and the impact of regeneration itself
- The amount of commercial floorspace

If the GLA approach was used in the PEACH area it would generate less social housing than a more nuanced model such as this. In our view, therefore, the GLA approach to costs and value, indicating GDV and potential planning gain, must be considered to be a minimum.

In general we note though that the estimation of costs and value at this stage of the policy process, at an area-wide level and over a long period of time can only be approximate. Wyatt and McAllister (2013) note that “Viability is very sensitive to differential changes in GDV and costs but current policy requires planning obligations to be tested for economic viability in forward planning documents, documents that remain in force for significant periods of time and often over entire market cycles”. This therefore means that “opportunities to obtain higher amounts of levy or obligation from more profitable sites are lost whilst, at the same time, more marginal sites may be made unviable” (Wyatt and McAllister, Univ of Reading Working Papers in Real Estate and Planning 09/13). In this regard we support regular review of the S106 agreements – including those which adopt a fast track approach - in relation especially to affordable housing offer.

Our more general concerns flow from this very vague (and necessarily so) assessment of viability at this stage of the strategic policy making process.

- (1) The GLA viability assessment methodology and standards is the absolute lowest level the community can accept
- (2) But the GLA approach must be strengthened to gain more public benefit and give back more value to the community e.g. a public debate over profit levels; more work on defining EUV [EXISTING USE VALUE] and having a proper debate about the premium which is due to developers and landowners; clawback/review clauses are a requirement and should be strengthened and regularly reviewed for efficacy; defining the social housing element which is expected very precisely and not falling back on intermediate housing to fulfil the Mayor’s electoral promises.
- (3) Furthermore, we strongly feel that the cause of achieving increased public benefit from land value uplift can only be strengthened by a more public approach, which we encourage the Mayor to enhance further. Many of the critical values are assumptions and highly contested eg benchmark land values; while both developers and LPAs draw on expert opinion, the resulting affordable housing offer is often just the result of negotiation, not an objectively established ‘maximum reasonable amount’. We feel this is important to open to democratic engagement to ensure that the Mayor’s policy priorities and the needs of Londoners are properly reflected in viability and development decisions. Thus we suggest the achievement of enhanced public value from development will be significantly improved by: complete transparency over finance; full viability assessment in plain english before a planning application is put out for public consultation; asking other housing developers whether they could make a site viable for policy compliant social/affordable housing; consider more strongly the potential for affordable housing and general planning gain contributions from the commercial sector BUT be more flexible for the social and community housing sector. We pointed out in our submission on Density that market prices of land (and thus ultimately Benchmark land values used in viability testing) would tend to be inflated by the removal of upper numerical limits on density. The absence of such limits will tend to make it harder to identify the “policy-compliant” transactions which the GLA (rightly) seeks to use in its evaluations of viability and we consider that the approach proposed will become less and less favourable to community interests as a result.

From the BLV’s in the “GLA note in response to Panel Note 9”, it’s pretty clear that very high (benchmark) land values (essentially the reasonable incentive

for land owners) are being assumed for the high house value areas. They range from £50m to £140m per hectare. This is where the trade-offs between planning obligations and land prices become most stark.

The justification in the GLA Main Report (8.2.1) reads

“In order to assess benchmark land values (BLVs) for the study land values for specific proposals have been reviewed. The BLV is used to determine whether a scheme is viable and is assessed by boroughs, and the GLA for applications referable to the Mayor, to ensure that these are in line with relevant guidance. This helps to ensure that land values reflect Development Plan policies whilst providing a competitive return to the land owner.”

Thus the LPVS methodology has been to look at what’s been done by boroughs and the GLA in the past and take the lead from these precedents. However, these precedents have tended to accept/reinforce very high land prices and have led to reduced planning obligations.

- (4) We have noted that in mixed development schemes, the non-housing element is usually excluded from the viability assessment for affordable housing, thus excluding a large element of potential cross-subsidy. In the PEACH model mentioned above including the development value from the offices by the Cross Rail station made a huge difference to the amount of social and affordable housing. How does the GLA deal with this? The potential for S106 is in danger of being reduced in mixed use schemes.
- (5) We also encourage the Mayor to explore other models for bringing forward development on low value land, as this is a wasted resource to achieve social housing, co-operative housing, and large scale affordable housing – other models than maximising profit share (at times this feels like crumbs from a developer’s table). We encourage an urgent review of possible alternative development models for low value land.