

TOOLKIT REPORT

ORCHARD ROAD, RICHMOND, TW9 4NY

HAREPATH ESTATES LLP

OCTOBER 2011

TOOLKIT VIABILITY REPORT

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3rd October 2011

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By email & post

Dear Mr Ackley



TOOLKIT REPORT – THE DAIRY, ORCHARD ROAD, RICHMOND TW9 4NY

We must state that this report is for the benefit of the London Borough of Richmond upon Thames, the Greater London Authority and Harepath Estates LLP only. No responsibility can be accepted to any third party for the whole or any part of its contents.

1.0 EXECUTIVE SUMMARY

1.1 This Toolkit viability assessment is in support of a proposed planning application to be submitted to the London Borough of Richmond-upon-Thames in respect of the above property.

1.2 We have appraised the following scheme:-

1.2.1 45 residential apartments

1.2.3 1,966 sq m (GIA) B1 Commercial space

1.3 We have appraised the impact on the viability of this proposal of providing 29% affordable housing by unit number, using the GLA's Development Control Model 2010/11. We have based this appraisal upon the proposed scheme contained within **Appendix 2**.

- In line with the Greater London Authority's (GLA's) strategic planning guidance for London, site-specific financial viabilities are a material consideration in determining how much and what type of affordable housing should be required in residential and mixed-use developments.
- As such, viability appraisals can and should be used to analyse and justify planning applications to ensure that Section 106 requirements do not make a scheme unviable.
- We understand that the GLA's logic is that, if the residual value of a proposed scheme is reduced to significantly below an appropriate **viability benchmark sum**, (in brief, the viability benchmark sum is arrived at following consideration of; unconditional purchase price paid, Existing Use Value / Current Use Value, plus a suitable landowner premium – either at the time of acquisition or current date, Alternative Use Value and/or Market Value) it follows that it is commercially unviable to pursue such a scheme, and the scheme is unlikely to proceed.
- If a scheme is being rendered unviable because of Section 106 requirements, it may be appropriate to look at reducing the burden of those requirements in order to facilitate viability.

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- Having appraised the proposed scheme the results confirm that:-
 - The proposed level of 29% affordable housing by unit number and additional Section 106 contributions of £224,087 represents more than the maximum which can be delivered without affecting scheme viability.
 - The appraisal (see **Appendix 9**) generates a residual value of £964,000. When compared with the viability benchmark of £1,525,000, it shows that the scheme is £561,000 short of being viable by normal commercial measurements of viability. When compared with the purchase price £2,750,000, it shows that the scheme is £1,786,000 short of being viable by normal commercial measurements of viability.
 - If a greater number of larger units were to be provided, this would further impact upon and adversely affect scheme viability.
 - In the current market if a developer was buying a site they would normally seek a return of at least 25% profit on cost in order to justify the risk of delivering the scheme given likely market and economic risks. In this instance, you have made an initial investment in both time and money to get to this stage and may be able to accept a lower than normal development profit. However, acceptance of a lower profit should be on an "ex gratia offer" basis in such a scenario as it would be a personal concession with respect to 'normal' profit levels.
 - The scheme would only be able to sustain the policy compliant level of affordable housing (50%) in Toolkit viability terms, if the residual value driven was in excess of the **viability benchmark sum**.

2.0 CLIENT INSTRUCTIONS

- 2.1 We have been instructed to examine the economic viability of this residential led mixed use scheme, so that the level of affordable housing and Section 106 contributions can be considered. We are pleased to provide our assessment using the Greater London Authority's – Affordable Housing - Development Control Toolkit (2010/11 version).

3.0 SITE DESCRIPTION

- 3.1 The site, on Orchard Road, runs south off Lower Richmond Road (A316). Garden Road runs east off Orchard Road. A fire station is situated to the north of the site and a Sainsbury's supermarket is located immediately to the west of Orchard Road, but is accessed from Lower Richmond Road.
- 3.2 The site is broadly rectangular in shape and measures approximately 0.3 hectares (0.74 acres).

4.0 SITE LOCATION

- 4.1 Please find a location plan at **Appendix 1**. Orchard Road is situated within the postcode district TW9, within the London Borough of Richmond upon Thames. The area is a mixture of residential, commercial and light industrial units.
- 4.2 North Sheen Rail Station (100 metres to the south west of the site) provides over-ground services on South West Trains via the Waterloo to Reading line with services running via Clapham Junction and Richmond. The nearest underground stations are Richmond to the west and Kew Gardens to the north, both are approximately 1.2km away. Both stations are served by the district line.

- 4.3 There are several bus routes along Lower Richmond Road, including routes 33, 337 and 493, which offer services to Tooting, Clapham, Putney and Charing Cross to the east.

5.0 PROPOSED DEVELOPMENT

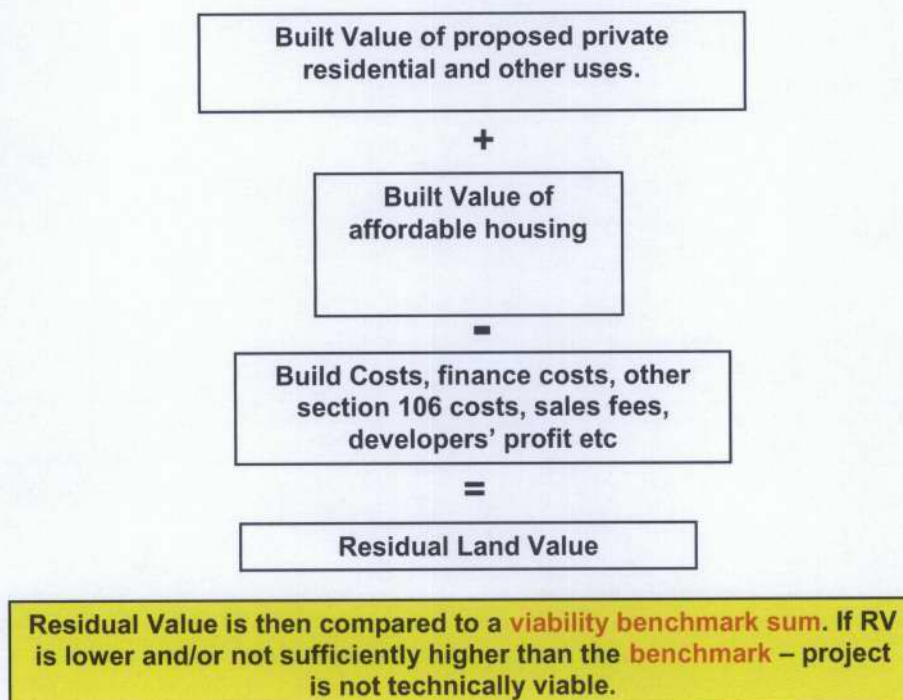
- 5.1 The proposals can be summarised as the redevelopment of the site to provide commercial floor space at basement, ground and first floors, 45 residential units ground to fourth floors and associated basement parking.
- 5.3 The scheme will provide pedestrian access via Orchard Road, whilst vehicle access to the car park will be from Market Road.
- 5.4 Plans of the proposed scheme are attached at **Appendix 2** and a schedule of accommodation at **Appendix 3**.
- 5.5 We have used the following mix in assessing the schemes viability.

RESIDENTIAL				
TENURE	UNIT TYPE	GIA SQ M	NO. OF UNITS	TOTAL GIA SQ M
Private	1B2P	50	12	600
Private	1B2P	51	4	204
Private	1B2P	52	3	156
Private	1B2P	53	4	212
Private	1B2P	54	3	162
Private	1B2P	57	1	57
Private	1B2P	68	1	68
Private	1B2PWC	67	2	134
Private	2B4P	80	1	80
Private	2B4P	82	1	82
Shared Ownership	1B2PWC	70	1	70
Shared Ownership	2B4P	70	2	140
Affordable Rent	2B4P	70	1	70
Affordable Rent	2B4P	75	4	300
Affordable Rent	3B5P	92	2	184
Affordable Rent	3B5PWC	107	1	107
Affordable Rent	3B5PWC	110	1	110
Affordable Rent	3B5PWC	117	1	117
TOTAL RESIDENTIAL			45	2,853
COMMERCIAL				
UNIT	UNIT TYPE	GIA SQ M	NO. OF UNITS	TOTAL GIA SQ M
Basement unit	B1	812	1	812
Commercial 1	B2	754	1	754
Commercial 2	B3	149	1	149
Commercial 3	B4	77	1	77
Commercial 4	B5	48	1	48
Ancillary commercial space	-	126	-	126
TOTAL COMMERCIAL			5	1,966

6.0 TOOLKIT VIABILITY ASSESSMENT METHODOLOGY

- 6.1 In line with the Greater London Authority's (GLA's) strategic planning guidance for London, site-specific financial viabilities are a material consideration in determining how much and what type of affordable housing should be required in residential and mixed-use developments.
- 6.2 As such, viability appraisals can and should be used to analyse and justify planning applications to ensure that Section 106 requirements do not make a scheme unviable.
- 6.3 We understand that the GLA's logic is that, if the residual value of a proposed scheme is reduced to significantly below an appropriate viability benchmark sum, it follows that it is commercially unviable to pursue such a scheme, and the scheme is unlikely to proceed.
- 6.4 If a scheme is being rendered unviable because of Section 106 requirements, it may be appropriate to look at reducing the burden of those requirements in order to facilitate viability.
- 6.5 The following issues are particularly relevant to viability:-
- The quantity of affordable housing.
 - The tenure split within the affordable housing between social rented, affordable rent and intermediate.
 - Grant funding on the affordable housing.
 - Cascade clauses related to grant, affordable housing quantum and tenure split.
 - 'Other' Section 106 costs (e.g. highways, education etc).
 - Optimum land uses within the development.
 - Family sized units.
 - Market conditions.
 - Timing of delivery.
 - Abnormal building costs.
 - Particular planning requirements.
- 6.6 The financial viability of development proposals is determined using residual land valuation methodology.

6.7 A summary of the residual valuation process is:-



6.8 The above land residual approach can be inverted so that it becomes a 'profit residual' based upon the insertion of a specific land cost (equivalent to the viability benchmark sum). By doing this, the focus is moved onto the level of profit driven by a scheme. This is, however, a purely presentational alternative.

6.9 Identifying an appropriate viability benchmark sum requires judgement bearing in mind that national planning guidance indicates that appropriate land for housing should be 'encouraged' to come forward for development.

6.10 There is some current debate about the extent to which purchase price paid (and related rolled up debt) should influence the choice of viability benchmark sum. The GLA seem to have de-emphasised the relevance of purchase price paid in their latest Toolkit guidance notes although previous versions indicated purchase price to be a valid benchmark sum influence. We see no reason for this change and, in fact, we see sensible reason for taking purchase price paid into greater account given recent land value falls as, without doing so, land will not be 'encouraged' to come forward for 'development'. Indeed, developers will be faced with unviable and blighted planning consents. As such, to ignore purchase price paid (unless unreasonable as at the time of purchase based upon prevailing market conditions and planning policies) would be bad for all stakeholders interested in the delivery (i.e. actual construction) of new housing.

6.11 We have considered several planning appeal decision commentaries (e.g. the 'Jericho' case) which point towards purchase price having been accepted in many cases as a reasonable viability benchmark in itself, or as a significant influence in arriving at a fair viability benchmark sum.

6.12 An appeal decision case we are aware of in this regard is APP/Y2620/A/08/2087479/NWF (decision date = 20/4/09) where the Inspector said:-

*"It seems to me that the price paid for a site, and the market value of the properties subsequently built there, must necessarily figure in any assessment of viability that underpins proposed affordable housing provision.
And the price paid for the site will reflect the purchaser's expectation of future market values."*

When market conditions are stable, then an experienced developer ought to be able to make reasonably reliable assessments of the value of future sales. But if the market becomes unstable then assessments of future viability of development sites will become less reliable. If residential property values fall in an unpredictable way between the time of site acquisition and the time that the development mix is determined, then the final development mix may be constrained in a way that could not reasonably have been foreseen at the time of site acquisition. Policy HO2 allows for this, because it incorporates the notion of viability".

6.13 In a letter from Steve Quartermain (Chief Planner - DCLG) dated 12th May 2009 to all local authorities in England entitled 'Planning for Housing and Economic Recovery', he promotes:-

- 'Reviewing existing sites to judge whether there are any actions that can be taken to unlock sites and allow development to go ahead';

and that;

- 'Now more than ever it is important to help authorities to ensure existing planning permissions are built out'.

6.14 In light of the letter from Steve Quartermain (see **Appendix 4**), we have e-mailed him to seek the DCLG's view on the extent to which purchase price paid should be taken into account in deriving an appropriate viability benchmark. A copy of his response to us can be seen in **Appendix 5**. We note that the DCLG is aware that 'many LAs currently use standard toolkits for assessing the viability of specific proposals, which allow for consideration of the actual cost paid for the site'.

6.15 In light of the narrative above, we consider it reasonable to use the higher of the following as the main influence (notwithstanding sensible judgement is still required on a case by case basis) in determining an appropriate viability benchmark sum within a viability assessment carried out as at the current date:-

- Unconditional purchase price paid (unless difficult to justify or more than, say, 5 years ago).
- Existing Use Value (EUV)/Current Use Value (CUV), as defined by the RICS, as at the time of 'unconditional' purchase, plus a suitable land owner premium (at least 15%), unless one defaults to Market Value, as defined by the RICS, in arriving at EUV because the property is vacant - in which case the RICS definition of EUV says one can default to MV.
- Current EUV/CUV plus a suitable land owner premium.
- Alternative Use Value ("AUV") as at the time of purchase (N.B. The RICS do not define AUV and the GLA's Toolkit guidance notes do not clearly define it. We assume it to mean the residual land value that would be driven by any reasonably foreseeable alternative scheme (in planning terms) which will probably involve no or less residential.
- Current AUV.
- Current rolled up debt (Bank debt and equity, but primarily Bank debt) against the site - reasonably, clearly and simply justified - and offset by any net income received!

(N.B. The 15% 'premium' levels referred to above reflect our belief that sites will not be encouraged to come forward for residential led re-development potential if vendors can only sell them at pure EUV levels. They require a premium to bring sites forward. The 15% premium also reflects, conservatively, guidance provided on premiums by appeal cases such as APP/L5810/A/05/1181361 and APP/G5180/A/08/2084559).

6.16 With regard to development profit (i.e. just one of many variables in a residual appraisal), the GLA's Toolkit default allowance is 17% of the total aggregate Market Value of the private residential units within a

residential scheme. Based upon current market conditions and the current development finance environment, this is probably insufficient. We believe this should be 25% on total cost, as a minimum, and possibly more for large complex projects. Within this appraisal we have assumed a development profit of 20% on total aggregate Market and Commercial Value.

- 6.17 Some developers may be willing and able to accept lower levels of development profit, if they can afford to, and/or if this does not prejudice their ability to raise development finance, and/or if they are relying upon market recovery to pull them into a position where they can feasibly commence construction of the whole scheme or part of it. For example, some developers may be able to accept a lower than normal profit if the prospective development risks are lower than normal. This might be the case where the proposed development is relatively straightforward in construction terms, where the units being built are of a sought-after/tried and tested standard, and/or where the market is strong. However, acceptance of a lower profit should be on an "ex gratia offer" basis in such a scenario as it would be a personal concession by the applicant with respect to 'normal' profit levels.

7.0 PURCHASE PRICE, EXISTING USE VALUE AND VIABILITY BENCHMARK

- 7.1 The existing building contains a total of 1,966 sqm (GIA) floor space at ground floor. We understand this is designated as B8 floor space, we have therefore applied a market rent of £53.82 psm (£5psft) and a yield of 8.5% on GIA. After allowing for purchasers costs at 5.8% this produces an EUV/CUV of £1.173m.
- 7.2 We have then added a further 30% (reflecting land owner premium) to the EUV/CUV producing a viability benchmark sum of £1.525m. We believe our approach to land owner premium is fair and reasonable given guidance (contained within the GLA Affordable Housing Development Control Toolkit 2010 guidance notes) which suggested a 20-30% premium is probably not unreasonable.
- 7.3 We understand that the purchase price of the site is £2.75m.
- 7.4 In light of the above we have adopted a viability benchmark sum of £1.525m; we have also included the impact on viability of adopting the purchase price for information purposes.
- 7.5 *Please note that this is not a formal valuation report and should not be relied upon as such.*

8.0 ECONOMIC MODELLING ASSUMPTIONS

- 8.1 In preparing the model we have generally used the default assumptions of the Toolkit, with the exception of the following items.

Section of Toolkit Model	Assumption Used
Basic Site Information	<ul style="list-style-type: none"> User defined number of dwellings.
Choice of Input Method	<ul style="list-style-type: none"> User defined dwelling types by quantity.
Unit Details	<ul style="list-style-type: none"> Floor areas for individual dwellings are an average of each type. Market values have been assessed using equivalent value/sq ft rates based on comparable new build developments in the area, second hand comparable transactions and discussions with local agents. Residential comparables are at Appendix 6.

Tenure	<ul style="list-style-type: none"> 29% affordable housing by unit. 77% Affordable Rented and 23% Shared Ownership by unit.
Build Costs	<ul style="list-style-type: none"> Build costs have been input on the residential units at £1,932 per NIA sq m and £1,000 per GIA sqm on the commercial space (including fit-out to Grade A specification). It is important to note that these figures are based on the total build cost including contractor overhead and profit. Demolition costs have been inserted separately within the toolkit under the Exceptional Development Costs section, whilst Architect, Structural Engineer, and Code For Sustainable Homes consultant fees have been omitted from the construction costs given the professional fees allowance. We have used build costs provided by Exel Group, (see Appendix 7).
Developer Return	<ul style="list-style-type: none"> We have assumed a 20% return on gross development value.
Planning Obligations	<ul style="list-style-type: none"> The planning obligation payments include a total budget of £224,087 within the toolkit appraisal, as advised by Indigo Planning.
Capital Contribution from Other Sources	<ul style="list-style-type: none"> We have anticipated that ground rents will be charged on the private market units at £250 per 1 bed unit and £300 per 2 bed unit per annum. Capitalised at a yield of 6% this produces a contribution input at Employer Contribution of circa £135,000.
Affordable housing	<ul style="list-style-type: none"> We have assumed no grant funding is available.
Commercial Element	<ul style="list-style-type: none"> We have assumed a rent of £161psm (£15psf) on the ground floor commercial units and £80.50psm (£7.50psft) on the basement commercial unit. We have made an assumption of 85% gross to net on overall commercial floor space in order to arrive at a net lettable floor area. We have applied a yield of 8% which generates a capital value of £2,629,525. Commercial comparables are at Appendix 6. Our assessment was made in consultation with our client's local specialist commercial advisor, Mark Belsham of Hargreaves Newberry & Gynell and our in house specialist commercial advisors. A Commercial Marketing report undertaken by HNG is at Appendix 8. We have not allowed for voids and rent free periods within this appraisal and reserve our right to review this area in further detail in the future. The commercial marketing report outlined above states that they would anticipate significant void periods, in excess of 12 months for a 5 year term certain.
Professional Fees	<ul style="list-style-type: none"> We have included professional fees at the toolkit default level of 12% of build costs.
Land Financing Costs	<ul style="list-style-type: none"> We have applied interest to the acquisition costs at 7% over a

	period of two years. This represents the anticipated period from acquisition, to obtaining planning permission and completing scheme construction.
Interest Rate	<ul style="list-style-type: none"> We have used an interest rate of 7%.

9.0 PRIVATE RESIDENTIAL VALUES

- 9.1 We have considered new build and resale comparables within TW9 and provide our research within **Appendix 6**.
- 9.2 We have chosen to use values using a comparative approach to valuation, having regard to the local housing market; both for new build and second-hand property. We have given brief consideration to the respective merits of this proposal against other schemes, in terms of size of units, accommodation provided, specification and finishes, car parking, the general external environment and access to local facilities. Given current market conditions and the limited number of recent transactions, we feel we have been robust in this regard.
- 9.3 We have valued each individual unit and have adopted the following range of private residential values, which assume a parking space is included within the toolkit appraisal.

Unit Type	Value
1 bed	£245,000 - £295,000
2 bed	£330,000 - £360,000
3 bed	£400,000 - £425,000

10.0 TOOLKIT RESULTS

- 10.1 The toolkit appraisal (see **Appendix 9**) generates a residual value of £964,000. When compared with the viability benchmark of £1,525,000, it shows that the scheme is £561,000 short of being viable by normal commercial measurements of viability. When compared with the purchase price of £2,750,000, it shows that the scheme is £1,786,000 short of being viable by normal commercial measurements of viability.

11.0 CONCLUSION

- 11.1 In our opinion and based on the economic viability assessment carried out in accordance with the defined guidelines of the Greater London Authority, it is evident that the scheme cannot sustain a policy compliant level of affordable housing. At 29% affordable housing (by unit) the scheme is still not technically viable. As such, the scheme cannot provide any more units as affordable housing or under a different tenure basis or indeed any additional Section106 contributions beyond those contained within the toolkit appraisal.
- 11.2 If a greater number of larger units were to be provided, this would further impact upon and adversely affect scheme viability.
- 11.3 In the current market if a developer was buying a site they would normally seek a return of at least 25% profit on cost in order to justify the risk of delivering the scheme given likely market and economic risks. In this instance, you have made an initial investment in both time and money to get to this stage and do not expect to see such a large return in bringing the project forward. As such we understand that you may well be able to accept a lower than normal development profit such as that delivered by this proposal. However,

acceptance of a lower profit should be on an "ex gratia offer" basis in such a scenario as it would be a personal concession with respect to 'normal' profit levels.

12.0 STATUS OF THIS REPORT

- 12.1 This is not a formal valuation report and values contained herein should not be relied upon as such. It has not been prepared in compliance with the RICS Appraisal and Valuation Standards.
- 12.2 This report is a GLA Toolkit based assessment of the proposed scheme for planning purposes based upon GLA Toolkit guidance.

Yours sincerely



MARK BREEN BA (Hons)
Associate Director
For and on behalf of Savills (L&P) Limited