

**ADAMS
INTEGRA**



**ECONOMIC VIABILITY ASSESSMENT
OF FUTURE
DEVELOPMENT IN CANTERBURY DISTRICT**

**Report for the consideration of
Canterbury City Council:**

This document does not constitute Council Policy

Final Report

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Appendix 2a - Is as per Appendix 2 but for schemes of flats only.

Appendix 2b - Is as per Appendix 2 but for schemes of houses only.

Appendix 3 - Shows a Summary of Residual Land Value (£) Appraisals for All Value Points; 0%, 25%, 30%, 35% and 40% Affordable Housing; 70% Social Rent/30% Shared Ownership; **CIL Level £40 and £60** at Low Density, Medium Density and High Density. The tables show actual RLVs, RLV as a % of GDV and RLV per hectare.

Appendix 3i - Shows a Summary of Residual Land Value (£) Appraisals for All Value Points; 0%, 25%, 30%, 35% and 40% Affordable Housing; 70% Social Rent/30% Shared Ownership; **CIL Level £80 and £100** at Low Density, Medium Density and High Density. The tables show actual RLVs, RLV as a % of GDV and RLV per hectare.

Appendix 3a - Is as per Appendix 3 but for schemes of flats only.

Appendix 3a-i - Is as per Appendix 3i but for schemes of flats only.

Appendix 3b - Is as per Appendix 3 but for schemes of houses only.

Appendix 3b-i - Is as per Appendix 3i but for schemes of houses only.

Appendices 4, 4i, 4ii, 4a, 4a-i, 4a-ii, 4b, 4b-i, 4b-ii - Are the same as Appendix 3 but at Code for Sustainable Homes Level 5.

Appendices 5, 5i, 5ii, 5a, 5a-i, 5a-ii, 5b, 5b-i, 5b-ii - Are the same as Appendix 3 but at Code for Sustainable Homes Level 6.

Appendices 6, 6i, 6ii, 6a, 6a-i, 6a-ii, 6b, 6b-i, 6b-ii - Are the same as Appendix 3 but at Code for Sustainable Homes Level 3

Appendix 7 - Shows Commuted Sums Residual Land Value (£) Appraisals for All Value Points.

Appendix 8 - Contains a summary of our property values and market research.

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Appendix 10 - Provides a Glossary of technical terms used throughout this study.

EXECUTIVE SUMMARY

This summary first seeks to briefly introduce and explain the study. It then provides a quick overview of the main study findings and goes on to outline the key recommendations.

For detailed information on the study methodology, results and conclusions it will be necessary to refer to the full text and appendices that follow this summary.

Background and Introduction

In the process of considering and developing its planning-led affordable housing policies Canterbury City Council have commissioned Adams Integra to:

- a) Inform the Council's strategy for delivering sufficient new homes by reviewing the portfolio of sites submitted under the Council's Strategic Housing Land Availability Assessment, and advising on the capacity of the market to deliver housing.
 - b) Recommend how calibration of policy for negotiating affordable housing can be optimised, to achieve the objectives of the Canterbury District Housing Strategy 2012-16.
 - c) Provide illustrative options-based CIL charges in the form of a draft charging schedule for housing and other types of development.
- 1 Government Policy at the time of publication of this work is as set out in the National Planning Policy Framework (NPPF) (published in March 2012).
 - 2 NPPF requires that Local Planning Authorities should set out their policy on local standards in the Local Plan, including requirements for affordable housing. They should assess the likely cumulative impacts on development in their area of all existing and proposed local standards, supplementary planning documents and policies that support the development plan, when added to nationally required standards. In order to be appropriate, the cumulative impact of these standards and policies should not put implementation of the plan at serious risk, and should facilitate development throughout the economic cycle. Evidence supporting the assessment should be proportionate, using only appropriate available evidence.
 - 3 NPPF states the following "*Pursuing sustainable development requires careful attention to viability and costs in plan-making and decision-taking. Plans should be deliverable. Therefore, the sites and the scale of development identified in the plan should not be subject to such a scale of obligations and policy burdens that their ability to be developed viably is threatened. To ensure viability, the costs of any requirements likely to be applied to development, such as requirements for affordable housing, standards,*

infrastructure contributions or other requirements should, when taking account of the normal cost of development and mitigation, provide competitive returns to a willing land owner and willing developer to enable the development to be deliverable.”

- 4 This report recognises that when assessing Plan Viability it can only provide high level assurance that the policies within the plan are set in a way that is compatible with the likely economic viability. It cannot guarantee that every development in the plan period will be viable, only that the plan policies will be viable for the sufficient number of sites upon which the plan relies in order to fulfil its objectively assessed needs.
- 5 The role of an assessment is to inform the decisions made by local elected members to enable them to make decisions that will provide for the delivery of the development upon which the plan is reliant.
- 6 This study is considered to be fully compatible with the NPPF in the context of building the evidence base for, and considering the affordable housing content of, the Core Strategy. It is to be considered as part of, and alongside, the Council’s developing wider evidence base, including information on the local housing market and housing needs, and information on the range of site sizes and types which are likely to come forward. We are aware of the new LGA guidance on Viability Testing for Local Plans, and the emerging Kent Planning Officers Group Methodology and consider that this report is broadly compatible with them.
- 7 The main objectives of this study are:
 - A District-wide affordable housing viability assessment for housing delivery over the lifetime of the Core Strategy.
 - A viability assessment which supports the affordable housing requirements that will be set out as policy in the emerging Core Strategy and other documents that will form part of the Local Plan.
 - An assessment of potential development scenarios of sites that reflect viability in the District overall, in terms of scope to deliver the affordable housing requirements.
 - An Economic Viability Assessment that takes account of different potential levels of Community Infrastructure Levy (CIL).
 - Consideration of specific factors that could impact significantly on the viability of schemes including residential values, Code for Sustainable Homes, Lifetime Homes, etc.

- 8 Maintaining the viability (in this sense meaning the financial health) of residential development schemes is crucial to ensuring the release of sites and thus a continued supply of housing of all types. The study addresses affordable housing that is required to be provided within market housing schemes and varying levels of CIL. This is through the existing established approach of setting site size thresholds (point(s) at which affordable housing policy is triggered) and proportions (percentages) of affordable housing to be sought at those points and also different levels of CIL.
- 9 The Council is intending to seek direct provision of much of the infrastructure required through the delivery of a series of larger development sites. The intention is that CIL will be used primarily to fund smaller more diverse, infrastructure schemes, such as generic transport improvements within the City, maintenance and improvement of open spaces, etc.
- 10 The study is based on carrying out a large number of developer-type appraisals. These use well-established "residual land valuation" techniques to approximate the sums of money which will be left available for land purchase once all the development costs, including profit requirements, are met (hence "land residual"). The appraisals are based on a widely applied calculation structure, common also to tools such as the Homes and Communities Agency (HCA) Economic Appraisal Tool.
- 11 A plan-wide test will only ever provide evidence of policies being 'broadly viable'. The assumptions that need to be made in order to carry out a test at plan level mean that any specific development site may still present a range of challenges that render it unviable given the policies in the Local Plan, even if those policies have passed the viability test at the plan level.
- 12 The basic study methodology is settled and tested, having been used in a wide range of local authority areas for this purpose. The assumptions, detail and particular application of calculations are varied to ensure local relevance. We make an appropriate strategic overview, as fits the Local Plan process, in a way that is both influenced by, and feeds back out to, the local characteristics and approach.
- 13 We vary the affordable housing assumptions across the range of appraisals. The outcomes inform our judgements on the likely suitability of various policy positions from a viability viewpoint. Having fixed development costs and profit requirements, we can see the impact on development viability caused by variations to the amount and type of affordable housing and differing levels of CIL. We can also consider the impact of variations to a wide range of other assumptions, as the study sets out.
- 14 Two of the key ingredients to ensuring viable development are sufficient land value created by a development (relative to existing or alternative use values,

and/or perhaps to an owner's particular circumstances) and adequate developer's profit in terms of risk reward and the profile of a scheme from a funder's point of view. Throughout the appraisals we maintain developer's profit whilst reviewing the scope to create land value depending on the affordable housing and other assumptions considered, and as those vary.

- 15 Affordable housing impacts on development viability mainly because it usually provides a significantly reduced level of revenue to the developer compared with market level sales values. Along with CIL it is viewed as a scheme cost which is largely passed onto the landowner by way of reduced land value. Also the Council currently expects new development proposals to achieve Code for Sustainable Homes Level 4 and meet Code Level 6 by 2015 and we assess the impact of Code Levels 3, 4, 5 and 6 on financial viability. It is these dynamics that we explore through this study, in considering the implications of a wide range of factors and costs on market residential development viability and its ability to provide affordable housing and CIL.
- 16 In considering all of this, we are looking for suitable policy targets, based on an appropriate balance between the opposing tensions of affordable housing need levels, the CIL charging schedule and scheme viability.

Property Market Characteristics and Viability Findings

- 17 Before commencing work on appraisals, Adams Integra researched the local residential property market to inform a range of appraisal assumptions, and to help set the context for considering the outcomes. This research is included within our Property Values Report, which is to be found at Appendix 8 to the full study document and includes information from the Hometrack system. It also includes a market commentary.
- 18 Through the run up to the study period, relatively poor property market conditions prevailed off the back of the economic recession triggered in late 2007. Whilst during the study period we have seen more mixed signs, and increased stability, there is still a significant degree of uncertainty around the market owing to the continued weak economic backdrop. This market uncertainty continues at the point of publishing this report.
- 19 In tune with the strategic overview needed through this study, we have considered a broad range of open market property sales value levels (house prices) that could relate to and drive new build housing schemes in The Canterbury District – as may be seen with varying location and/or through time with varying market conditions.
- 20 This exercise led to the formation of 5 ascending Value Points (numbered 1 to 5) in all, to describe the overall range of assumptions on values; i.e. from £1772/m² (about £164/ft²) to £4,000/m² (about £371ft²).

- 21 Value Point 1 shows a level below that which we considered to be at the lower end of the market in order to allow for any falls in sales prices. Value Point 5 is level above that which we found at the higher end of the market.
- 22 These Value Points covered the extremes of the range typically seen at the point of the study.
- 23 The study acknowledges that local variations in value levels are going to be key to site specifics, but this approach sets a background for that level of consideration and is appropriate for strategic policy development.
- 24 Reviewed alongside the wide range of factors considered and also treated as variables within the range of study assumptions (for example, including wider planning obligations, affordable housing mix, Code for Sustainable Homes, developers profits and land values) overall the results create a mixed picture of development viability. This includes scenarios where typically strong local values often produce good viability outcomes, but also where lower values and/or increased overall burdens on schemes reduce what they are likely to support by way of planning obligations packages.
- 25 We consider that in the overall context of the District - with varying values - and assuming variable market conditions over the Local Plan period a **30%** affordable housing headline would be a sufficiently challenging and appropriately pitched target generally. A range of other requirements needs to be considered alongside affordable housing. Beyond this level, any target would be potentially too ambitious in our view – given the range and direction of wider planning obligations and other development costs. Adding to this picture, affordable housing provision needs to be about quality and mix, and not just numbers.
- 26 Our resulting focus is around a headline of **30% affordable housing**, as a target level for the majority of sites within the District. To accompany this, and act as a balancing factor, we consider there to be important scope to firm up on an approach which seeks affordable housing from a wider range of schemes through lowered thresholds universally.
- 27 We also give support to the potential for using carefully judged financial contributions for affordable housing as an additional enabling tool, particularly from the very smallest schemes (fewer than 6 units) but also from other schemes in areas where the Council may consider that a financial contribution could be better spent to help enable the greater provision of affordable housing across the District as a whole.
- 28 In addition, we explore the potential for schemes that fall in the higher value areas such as in Canterbury and Whitstable to bear an increased proportion of

affordable housing alongside CIL. Alongside this we recognise that schemes that fall within Value Points 1 and 2 are on the cusp of viability margins.

Overview of Main Recommendations

The SHLAA

- 29 **The Council commissioned the DTZ Report “Canterbury LDF Housing Options”, which was undertaken for the draft Core Strategy, which took a higher level approach to the marketing, viability and delivery issues.**

The actual number of units delivered, though, is dependent upon the market (and this is an area that is difficult to comment on) and may also be influenced by any policies that may serve to regulate the timing of release of sites.

- 30 We have looked at the assessment process, the site survey process and the assessment of whether and when sites may be developed and find it to be a sound and robust document.

- 31 In our opinion the findings of the SHLAA are sound and robust and show that there is enough land available to more than deliver the required number of dwellings.

- 32 With regard to the capacity of the market to deliver these housing numbers there is evidence of a need for new housing to be built. There is a huge shortage of new houses nationally and this is the case in the Canterbury District and Kent as a whole.

- 33 It is our professional view that the market for flats is experiencing a downturn and the emphasis currently is on developing houses.

Affordable Housing

- 34 **A headline affordable housing target of 30% to be provided on-site applicable to schemes of 7 or more dwellings.**

- 35 **For schemes of between 1 and 6 inclusive units either on-site provision or a financial contribution be sought in lieu of providing affordable housing on-site, and that this be calculated using the methodology outlined below and will be broadly equivalent to on-site provision (retaining 30% affordable housing where applicable).**

The suggested calculation seeks to equate the financial contribution to the land value of the relevant dwelling plots (those that would have been made available for on-site affordable housing).

It is beyond the remit of this study to comment on the planning policy scope or wider merits of an approach to seek financial contributions towards meeting affordable housing needs from the smallest sites, but to inform only on the development viability aspects. There are potential practical advantages of requesting financial contributions from the smallest sites rather than adhering to on-site provision. There can be issues with affordability, integration, management and the like in relation to providing affordable housing on small sites. This policy approach could have practical merits with those issues in mind. If those concerns are removed through the use of financial contributions in lieu of on-site provision, then dependent on the scale of the payment being appropriately judged there is unlikely to be a pure financial viability issue – subject as normal to any existing/alternative use barriers and the normal negotiation process where necessary.

In our view, the most appropriate route more generally is to look at land value. In essence this involves calculating how much it would cost to go elsewhere and replace the land on which the affordable housing would have been provided on-site. This is the basis we have assumed.

We work through our calculation methodology below, which is based on a formulaic approach to approximating the land value that needs to be replaced elsewhere, and then allowing also for the cost of acquiring and servicing that land. We start by taking the value of the land as if no affordable housing were required on-site, calculated as a percentage of the market sale value of a property. This percentage would reflect the pre-affordable housing (0%) residual land value results, as taken from this study.

For this purpose we have applied a proportion of **20%** of the relevant property or properties Open Market Value (OMV) as the residual land figure. This was derived from all relevant 0% affordable housing appraisals from sites in range 2 to 100 units.

An allowance is added for acquisition and (potentially) for servicing costs that would need to be borne in the case of replacing the land elsewhere in the market.

In summary, the financial contribution is arrived at by the following steps:

- a) Open market value (OMV) of the housing units on-site.
- b) Multiply by the residual land value percentage. We have used 20%.
- c) Add 15% of the result of a x b to reflect site acquisition and servicing costs. This gives the per unit sum.
- d) Apply to the relevant site number and proportion (in this case 30%).

Worked example to illustrate the above:

- A scheme of 3 No 3-bed houses selling at £190,000 each
- Total GDV = 3 x £190,000 = £570,000
- x by RLV (£570,000 x 20%) = £114,000
- x by 15% for fees (£114,000 x 115%) = £131,100
- x 30% affordable housing requirement (£131,100 x 30%)
- Financial contribution = **£39,330**

36 **Where appropriate the Council will, in exceptional circumstances, accept a financial contribution in lieu of providing some or all the affordable units on-site which will be calculated as set out in the paragraph above.**

37 **In areas that may be typically lower value that are shown as Value Points 1 and 2, in our opinion it would not be appropriate to set lower rates bearing in mind that those locations may also “host” some higher value schemes. It is our opinion that individual schemes that are in these lower value areas should be looked at on a scheme by scheme basis. Where it can be shown that a residential scheme has particular viability issues then a case should be put forward by the developer which should then be independently assessed.**

38 The cost of any scheme-specific viability assessment should be funded by the applicant.

39 In practice, residential values patterns are not well defined. We consider that a clear, straightforward District-wide approach would be more appropriate than much more complicated alternatives.

40 **The financial contributions approach will be a useful additional enabling tool for the Council as part of its overall approach** – especially during periods (as at present), of uncertain grant funding (HCA or other investment).

41 **A target affordable housing tenure mix of 70% social rented: 30% suitable intermediate tenure;** not for rigid site-by-site application, but in terms of setting the overall expectations and guiding delivery. This is consistent with HCA guidance in recent years and concurs with the East Kent Strategic Housing Market Assessment (2009) which also recommends that 70% of new affordable homes should be for rent and 30% shared ownership and this has been included in the current housing strategy. It is a tenure split

that has been used widely to help provide mixed communities and mixed tenure developments.

- 42 In all cases the **policy positions should be set out as clear targets**, to help inform land value expectations and form the basis for a continued practical, negotiated approach.
- 43 Policy wording will **need to acknowledge the relevance of considering development viability** on case specifics.
- 44 The Council will **need to consider the mathematical subtleties of its selected approach** – for example, how numbers rounding and net/gross (new dwellings numbers) application affects the working of the policy positions, particularly for smaller sites where such factors will tend to have a greater influence on outcomes.
- 45 The build costs used in the assessments assume that the flats and houses are built to Code for Sustainable Homes Level 4.
- 46 The Council have asked that we also consider the impact of Code Levels 5 and 6 on financial viability.
- 47 Information relating to the cost of achieving the two scenarios above have been taken from the Communities and Local Government document – *"Code for Sustainable Homes - A Cost Review" – Updated August 2011.*

The findings of the report look at many different scenarios but taking average figures and using a base level costing of Code for Sustainable Homes Level 4 the following extra over build costs should be applied to a typical 3 bed terraced house at 85 m²:

- i. Code Level 5 - £180/m²
- ii. Code Level 6 - £290/m²

The effect of the above costings on viability mean that the overall percentage can be maintained for Code Level 4. However, the increased costs associated with Code Level 5 mean that the affordable housing requirement would need to be reduced to an overall provision of 0% and the CIL would need to be reduced to zero. For Code Level 6 the same would also apply due to the even higher build costs.

We also looked at the effect of only building units to Code Level 3. The uplift from Code Level 3 to Code Level 4 in extra over build costs would be in the region of £88/m². The decreased costs associated with Code Level 3 would mean that the affordable housing requirement could be increased to an overall

provision of 35% and the CIL could potentially be increased from £40/m² to £60/m².

Lifetime Homes

- 48 The Council currently expects 20% of affordable homes to be built to Lifetime Home Standards. We have been asked to appraise the impact of the 20% requirement and also the impact of constructing all affordable homes to Lifetime Home Standards on the viability of new affordable homes. In addition, we have been asked to appraise the impact of requiring 20% of market housing to be built such standards.
- 49 There have been a number of studies into the costs and benefits of building to the Lifetime Homes standard. These have concluded that the costs range from £545 to £1,615 per dwelling, depending on: the experience of the home designer and builder; the size of the dwelling (it is easier to design larger dwellings that incorporate Lifetime Homes standards cost effectively than smaller ones); whether Lifetime Homes design criteria were designed into developments from the outset or whether a standard house type is modified (it is more cost effective to incorporate the standards at the design stage rather than modify standard designs); and any analysis of costs is a 'snapshot' in time. The net cost of implementing Lifetime Homes will diminish as the concept is more widely adopted and as design standards, and market expectations, rise. The most significant factor when considering costs was whether the home had been designed to incorporate Lifetime Homes criteria from the outset or whether a standard design had been modified. In 1997 Sangster[1] looked at costs when incorporating the Lifetime Homes standard from design stage and found that extra costs could be as low as £90 for a three-bedroom, five-person social rented house, and £100 for the same size house in the private sector. The study found that most of the Lifetime Homes design criteria cost nothing when designed in at the beginning. The inclusion of a downstairs toilet, with the possibility to incorporate a shower later, incurred the highest cost. With the exception of the two-bedroom, four-person house, the extra cost associated with the toilet was £69.

Cyril Sweett, when considering the implications of moving from EcoHomes Very Good to the draft Code for Sustainable Homes (CfSH), concluded that Lifetime Homes did not have a significant impact on overall project costs because the requirements of the revised Part M of Building Regulations now require many of the same considerations to be addressed as a matter of course.

It is our recommendation that if the Council chose to have all new housing built to Lifetime Homes then it would not have a significant negative impact on scheme viability.

CIL Requirements

- 50 Rather than variation by area (locality), in carrying out the research for this study we developed the view that the key variable characteristics associated with different types of development require an approach that moves away from a single CIL rate. Development type rather than locality should be the key driver.
- 51 Value Points 1 and 2 produce residual land value (RLV) outcomes which show no scope for CIL payments. In fact, in most cases the results are in significantly negative territory indicating scenarios that are not even marginal in terms of being potentially viable without major adjustment to assumptions.

Residential Findings

- 52 Value Points 3 and above begin to produce some marginal results. This indicates primarily the level at which schemes start to become viable. The various different residential scenarios were tested at different levels of CIL (£40, £60, £80 and £100 per m²) and at each level the schemes in Value Points 3 and above are shown to be viable at 30% affordable housing when compared to benchmark land values.
- 53 The more positive outcomes shown in Value Points 3-6 could quickly be eroded by increased cost assumptions or abnormal site issues, etc. Increased costs or a fall in the residential values will also have an effect on viability.
- 54 In Value Point areas 1 and 2 developments are currently unviable whether or not CIL is levied. The imposition of CIL will therefore not affect the prospects of these sites being delivered. Where appropriate schemes can be looked at on a site-specific basis and re-tested with lower proportions of affordable housing allowing CIL contributions to be secured.
- 55 The Government Guidance confirms that the CIL scope should not be pushed to the limits of viability, but Regulation 14 requires that a charging authority, in setting CIL rates, *'must aim to strike what appears to the charging authority to be an appropriate balance between' the desirability of funding infrastructure from CIL and 'the potential effects (taken as a whole) of the imposition of CIL on the economic viability of development across its area'.*
- 56 **We would therefore suggest a rate of £40 per m²** to allow an adequate buffer for site-specific factors and recommend that the Council does not go beyond this level in considering its draft charging schedule.
- 57 This relates reasonably well to the Council's existing largely formulaic basis for seeking and securing a range of planning obligations and contributions; most of which may be replaced by the wide-ranging scope of CIL in covering all but

very site-specific matters (affordable housing and perhaps particular site-specific issues such as dedicated highways improvements). A small residual allowance of £500 per dwelling has been made within our appraisals for any matters that will not be covered by the CIL and still need to go in to a S106 agreement along with affordable housing obligations (where applicable).

- 58 There will be lower value schemes and localities where developments struggle in viability terms, even without any significant CIL contribution. So far as we can see, no lower level set for CIL could ensure the deliverability of these schemes on a reliable basis, or make sure that some levels of CIL were always collectable.
- 59 In terms of methodology, we adopted standard residual valuation approaches to make appropriate comparisons and evaluations. However, due to the extent and range of financial variables involved in residual valuations, they can only ever serve as a guide. Individual site characteristics (which are unique), mean that blanket requirements and conclusions must always be tempered by a level of flexibility in application of policy requirements on a site by site basis. It is therefore essential that levels of CIL allow a sufficient margin to allow for these variations.

Sheltered Housing

- 60 The viability of sheltered housing is largely similar to that of general residential as sales values reflect local market levels. However, there are two factors which may adversely affect viability. Firstly, the rate of sale of sheltered housing schemes is generally slower than for mainstream residential, due to the more limited market catchments. Developers consequently incur greater interest costs on land and build costs. Secondly, sheltered housing schemes include a significantly higher level of communal space to accommodate social areas and other facilities.
- 61 We would therefore recommend that the Council has regard to the CIL rates for general residential and applies a rate of **£40 per m²** to sheltered housing but is aware that, while this, together with 30% affordable, housing may both be viable, there may be site-specific viability issues in relation to the affordable housing element due to these special factors.

Future proofing the findings of the report over the plan period to 2028

- 62 The Value Points system allows us to understand viability as prices move. For example, in a rising market the values in Value Point 3 might rise to Value Point 4, or fall to Value Point 2 in a falling market. The Value Points table can be kept as a reference tool for this purpose, so that in two years' time the Council could undertake a review of prices in the market place and see where they sit on the table.

63 This does not, of course, take into account any movement in build costs, but it is movements in sales values that will have the greatest bearing on viability, assuming no additional abnormals.

64 This report is a snapshot in time which based on research will inevitably become outdated. It is our opinion that a review should be carried out in 2016 of viability to ascertain whether the market has moved significantly (either up or down) and whether the affordable housing percentage should be adjusted. Further reviews should be carried out in 2021 and 2026.

Executive Summary ends