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17 April 2015

Dear Sirs

Southwark v Information Commissioner and Lend Lease and Glasspool – EA/2013/0162

Further to our e-mail received earlier today.

In accordance with the First-Tier Tribunal decision notice of 10 March 2015, please find enclosed a copy of the document for disclosure.

Yours sincerely,

Norman Coombe
Head of Corporate Team

Legal Services

STRICTLY PRIVATE & CONFIDENTIAL

9 May 2012

Elephant & Castle – The Heygate Masterplan

VIABILITY ASSESSMENT

Prepared for:

Lend Lease (Elephant and Castle Limited)

Prepared by:

MARK BREEN | **SARAH CURTIS MRICS**

Director | **Surveyor**

For and on behalf of:

Savills L&P Limited
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1. Executive Summary

1.1 This viability assessment has been prepared and submitted by Savills, on behalf of Lend Lease (Elephant and Castle) Limited (LL) (the "Applicant"), to support an outline planning application for The Heygate Masterplan in Elephant and Castle (the "Site").

1.2 This viability assessment relates to the Heygate Estate, a 1970s housing estate owned by Southwark Council, which provides 1,107 residential units, located within several buildings of up to 12 storeys in height. The majority of these apartments are now vacant.

1.3 The proposed development comprises a single outline planning application for the demolition of all structures on the Site and its redevelopment for a mix of uses. Accordingly, planning permission is being sought for the following development:

"Demolition of all existing structures and bridges and redevelopment to provide a mixed use development comprising residential (C3), retail (A1-A5), commercial (B1), leisure and community (D1 and D2), and energy centre (sui generis uses), new landscaping, park and public realm, car parking, means of access, and other associated works."

1.4 Lend Lease have committed to deliver a minimum of 25% Affordable Housing within The Heygate Masterplan and wish to express their determination to meet this vision through examining the financial viability of the proposals and the potential value enhancement options.

1.5 This viability assessment forms part of the above planning submission.

1.6 The following scheme (which represents an Illustrative Masterplan as submitted) has been appraised:-

- 2,462 residential units comprising 123 studios, 830 one bedroom, 1,260 two bedroom and 249 three bedroom flats;
- 25% affordable housing provision by habitable room split as 50% Shared Ownership and 50% Social Rented by habitable room. This equates to 1,892 private units, 287 Shared Ownership units, and 283 Social Rented units;
- Retail (A1-A5), Office (B1), leisure and community (D1 & D2) uses; and
- A maximum of 616 car parking spaces for all uses including residential, commercial, retail, community, leisure and visitors. An appropriate level of car club spaces are also to be provided within the Development. The provision will be reviewed as the development evolves through the site-wide Travel Plan.

1.7 In line with; the adopted National Planning Policy Framework (NPPF) and the Greater London Authority's (GLA's) strategic planning guidance for London, financial viability is a material consideration in determining planning requirements.

1.8 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.

1.9 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, at least 15-30% above Existing Use Value/Current Use Value, 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.

1.10 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.

1.11 Due to the scale and significance of this proposal as well as the long term involvement of both the Applicant and the Council, discussions surrounding the economic modelling of the redevelopment are well established. It is our understanding that, throughout the pre-application process, Lend Lease have provided the Council and a number of independent reviewers with copies of their bespoke development appraisal model in order to inform their ability to contribute towards strategic infrastructure.

1.12 As such, the format of Lend Lease's bespoke development appraisal model has been reviewed and accepted by; DTZ on behalf of Transport for London (TFL) and the GLA, and Drivers Jonas Deloitte (DJD) on behalf of SC Property. We also understand that the model and its functionality have been audited by Price Waterhouse Coopers (PWC) on behalf of SC Property.

1.13 Further to this in December 2011 the District Valuer Services, who have been instructed by Southwark Council as their independent reviewer for the viability assessment, reviewed the Lend Lease model and accepted it as a suitable development appraisal on which to test the viability of the proposal.

1.14 As such, in appraising the impact that providing affordable housing units alongside further section 106 contributions has on the viability of the scheme with a view to establishing what quantum and type of affordable provision and section 106 obligations the scheme could support (whilst remaining commercially viable), we have had regard to the bespoke financial appraisal Model 6.24 (the Model) provided to us by the Applicant.

1.15 Having considered the results of the financial appraisal we can confirm that :-

- The proposed scheme in its current form with the level of planning obligations detailed drives a developer's return of profit on cost and IRR, when compared to the viability benchmark this is not commercially viable.

- In order to address the viability gap identified by the appraisal, there are a number of options which could be considered these include (but are not limited to):

  1. Enhancing the value of the proposed affordable housing;
  2. Securing grant funding for the scheme;
  3. Reducing the financial section 106 obligations; and
  4. Reducing the quantum of affordable housing.

1.16 In the first instance, in line with point 1 above, we would advise that the Applicant, in conjunction, with Southwark Council consider the following value enhancement options:

<u>Social Rented</u>

Convert to Affordable Rent at 80% of Market Rent on all rented units.

Convert to Affordable Rent at 80% of Market Rent on the 1 and 2 bed rented units and 65% of Market Rent on the 3+ bed units.

Convert to Affordable Rent at 65% of Market Rent on all rented units.

Convert to Affordable Rent at 65% of Market Rent on the 1 and 2 bed rented units and Target Rent on the 3+ bed units.

<u>Intermediate</u>

All Intermediate housing provided as discount to market sale at 85% of Market Value.

All Intermediate housing provided as discount to market sale at 75% of Market Value.

All Intermediate housing provided as Shared Ownership units compliant with the GLA's adopted policy on affordability thresholds.

All Intermediate housing provided as Shared Ownership units compliant with the mid point between Southwark Council's emerging policy and the GLA's adopted policy on affordability thresholds.

1.17 Once the value enhancements options have been fully examined, should there be a requirement for further redress to the viability gap we would advise that the Applicant seek guidance from Southwark Council and the GLA with respect to points 2-4 above.

2. Introduction

2.1. Client Instruction

This viability assessment has been prepared and submitted by Savills, on behalf of Lend Lease (Elephant and Castle) Limited (LL) (the "Applicant"), to support an outline planning application for The Heygate Masterplan in Elephant and Castle (the "Site").

We have been instructed to examine the development economics of the submitted scheme, so that the level of affordable housing and section 106 contributions can be considered. We have been provided with a financial appraisal of the scheme to consider (E&C Model 6.24) which relates to an Illustrative Masterplan that has been the subject of pre-application meetings and is illustrated within the application documentation.

2.2. Confidentiality

Due to the commercially sensitive nature of some of the information provided as part of the viability assessment, this report is provided on a strictly private and confidential basis. We understand that the report will be submitted to Southwark Council and the Greater London Authority (GLA) as a supporting document to the planning application. The report must not be recited or referred to in any document, or copied or made available (in whole or in part) to any other person (save the consultants instructed by the Council and the GLA to review the report) without our express prior written consent.

2.3. Report Limitations

Although this report has been prepared in line with RICS valuation guidance, it is first and foremost a supporting document to the planning application in order to inform section 106 negotiations. Therefore it should be noted that, as per Valuation Standards 1 of the RICS Valuations Standards March 2012 Incorporating the International Valuation Standards – Global and UK Edition, advice given expressly in preparation for, or during the course of negotiations or possible litigation does not form part of a formal "Red Book" valuation and should not be relied upon as such.

2.4. Date of Appraisal

The Date of Appraisal is the date of this report.

3. Subject Site

3.1. Site Location

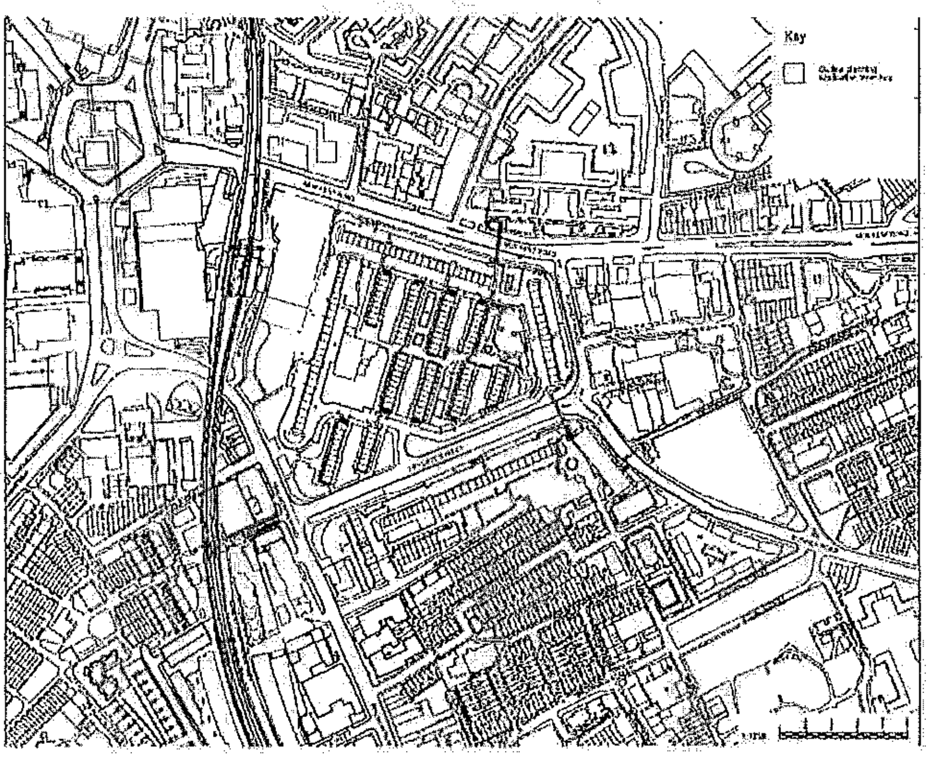
3.1.1. The Site is located in Elephant and Castle, within the administrative boundary of Southwark Council (SC). The Site is bound by:

- New Kent Road (A201) to the north;
- Rodney Place and Rodney Road to the east;
- Wansey Street to the south; and
- Walworth Road (A215) and Elephant Road to the west.

Heygate Street bisects the Site with junctions to Walworth Road to the west and Rodney Place and Rodney Road to the east.

3.1.2. The application boundary is defined by plan reference P01 Rev PO (**Appendix 1**) and set out below:

Figure 1



3.1.3. The Site represents a significant regeneration opportunity for SC within the Elephant and Castle Opportunity Area.

3.2. Site Description

3.2.1. The Site is predominantly occupied by the Heygate Estate. Owned by Southwark Council, this 1970s housing estate provided 1,107 residential units within the application boundary, located within several buildings of up to 12 storeys in height. The majority of these apartments are now vacant.

3.2.2. The Site extends to 9.71 hectares (23.98 acres).

3.2.3. A breakdown of the existing Heygate Estate residential buildings within the red line plan for this application is provided below:

Table 1

BUILDING	UNIT SIZES					
	Bedsits	1 bed	2 bed	3 bed	4 bed	TOTAL
Kingshill	0	119	109	0	0	228
Wansey Street	0	0	4	15	0	19
Swanbourne	0	88	22	0	0	110
Ashenden	0	198	44	0	0	242
Claydon	0	106	110	0	0	216
Marston	0	56	48	0	0	104
Cuddington	0	0	19	39	22	80
Chearsley	0	0	21	34	17	72
Risborough	0	0	10	16	10	36
TOTAL	0	567	387	104	49	1,107
% of stock	0%	51%	35%	9%	4%	100%

3.2.4. In addition to the Heygate Estate, the Site incorporates a number of other land uses, and areas of open space. These include:

- Garages located beneath the residential units and pedestrian walkways;
- Playgrounds and sports areas;
- Gardens, including a number of trees and the Elephant Road Park;
- A former petrol station (located to the southwest of the Site);
- Boiler House;
- A small number of retail units and community facilities; and Crossway Church on New Kent Road.

3.3. The Surrounding Area

3.3.1. The land uses surrounding the Site are primarily residential, with residential land uses to the north, south, and southwest, including the Draper, Newington and Alberta Housing Estates to the southwest; Nelson and Browning Estates to the south; and Rockingham Estate to the north. Residential properties on Wansey Street and Brandon Street are located directly opposite the Site to the south.

3.3.2. Student accommodation is located to the southwest and north of the Site, and the mixed use 44 storey Strata Tower is located to the southwest. There are a number of other land uses, together with significant transport infrastructure, that are also located within the vicinity of the Site. These include:

- Retail and leisure, including the Elephant and Castle Shopping Centre to the west of the Site, comprising a supermarket and other retail units; the London Palace Superbowl bowling alley; Bingo Hall; the Charlie Chaplin Public House; the Coronet Theatre; cafes, restaurants and hot food takeaways; and an external market space.
- Retail uses, including pubs, bars, cafes; restaurants; a night club and takeaway establishments are located to the south and north of the Site, primarily on Walworth Road, Elephant Road in the railway arches and New Kent Road.
- Oakmayne Plaza to the immediate north west – currently under construction for a mixed-use development incorporating retail, leisure, residential, and student accommodation uses.
- Education facilities including:
    - Victory School to the east;
    - St John's Walworth Church of England Primary School to the south;
    - Globe Academy to the north;

- Crampton School to the southwest;
- London College of Communication to the west; and
- London South Bank University to the northwest.

- Office and business uses, including the 16 storey 'Hannibal House' building above the Elephant and Castle Shopping Centre and the Department of Health building located within Skipton House to the north west of the Site.
- Light industrial uses within the arches beneath the raised railway viaduct to the west of the Site, beyond Elephant Road.

4. Proposed Development

4.1. Planning Application

4.1.1. This section should be read in conjunction with the Development Specification which is submitted in support of the application and defines and describes the principal components of the Development.

4.1.2. The Development comprises a single outline planning application for the demolition of all structures on the Site and its redevelopment for a mix of uses. Accordingly, planning permission is being sought for the following development:

"Demolition of all existing structures and bridges and redevelopment to provide a mixed use development comprising residential (C3), retail (A1-A5), commercial (B1), leisure and community (D1 and D2), and energy centre (sui generis uses), new landscaping, park and public realm, car parking, means of access, and other associated works."

4.1.3. The proposed scheme is to be developed over approximately a 13 year development timeline. The scheme Masterplan and Block Drawings are at **Appendix 2**.

4.2. Uses and Amount of the Development

4.2.1. The Development will deliver a vibrant mix of uses to complement the new and existing residential community, such as shops, bars, cafes and restaurants, business, community, cultural and leisure uses.

4.2.2. In summary, the application seeks permission for a maximum total of 330,741 sqm GEA floorspace. Table 2 below defines the maximum and minimum floorspace figures for each category of land use proposed.

Table 2

Land Use	Use Class	Minimum GEA (m2)	Maximum GEA (m2)
Residential	C3	160,579**	254,400**
Retail	A1/A2/A3/A4/A5	10,000**	16,750**
Business	B1	2,000	5,000
Community and Culture	D1	1,000	5,000
Leisure	D2	1,000	5,000
Sui Generis / Energy Centre	Sui Generis	500	925
Sub –Total	-	175,079	287,075
Parking; Servicing; Plant; Storage	-	34,854	43,666
TOTAL	-	**209,933**	**330,741**

***Please see notes on the measurement of residential and retail GEA attached to Table 4.1 of the Development Specification which is attached at **Appendix 3**.*

4.2.3. The application seeks permission for a maximum level of residential floorspace of 254,400 m2 (GEA) and a minimum level of 160,579 m2 (GEA). This will be distributed across the development and can accommodate between 2,300 and 2,462 units depending on the precise mix and unit sizes.

Character Areas

4.2.4. The Site is sub-divided into five specific character areas which have been established to create a variety of experience and richness to the Development and determine the functions of the individual development plots. The five character areas are: The Park; Walworth Road; New Kent Road; Walworth Local; and Rodney Neighbourhood.

Development Plots

4.2.5. The Site is further sub-divided into 12 individual development plots (H1-H7, H10, H11a, H11b, H12, and H13) plus a park pavilion (PAV1). The individual development plots contain a mix of residential and other lands uses, and are of varying heights and sizes according to the character area in which they are located.

Open Space

4.2.6. In addition to the built floorspace set out above, the Development includes significant areas of open space, including a new park, gateway spaces, and new streets. Mature trees will be retained where possible and complemented with new landscaping. The Development will provide a minimum of 45,286 sqm (4.53ha) of publically accessible realm.

Car Parking & Cycle Parking

4.2.7. The Development will provide a maximum of 616 car parking spaces and a maximum of 3,136 cycle parking spaces for residents, workers, and visitors to the Development. Further details on parking numbers are set out within the Development Specification, Transport Assessment, and Travel Plan, which is to be submitted as part of the outline planning application.

Proposed Residential Accommodation Schedule

4.2.8. An accommodation schedule for the Illustrative Masterplan is attached at **Appendix 4**. The following table details average unit types and sizes upon which the financial appraisal is based.

Table 3

Tenure	Studios	1 Beds	2 Beds	3 Beds	Total
Private	123	658	1,013	98	1,892
Intermediate		89	129	69	287
Rented		83	118	82	283
Totals	123	830	1,260	249	2,462

4.2.9. All residential development will be designed where possible to meet the minimum standards of the London Plan 2011 and Southwark Residential Design Standards.

4.2.10. Affordable housing in the proposed development will comply with the following minimum dwelling sizes set by Southwark Council within their Affordable Housing SPD Draft June 2011:

Table 4

Development type	Dwelling type (bedroom/persons)	Essential GIA (sqm)
Flats	Studios	36
	1b2p	50
	2b3p	61
	2b4p	70
	2b average	66
	3b4p	74
	3b5p	86
	3b6p	95
	3b average	85
	4b5p	90
	4b6p	99
	4+b average	95
2 storey houses	2b4p	83
	3b4p	87
	3b5p	96
	3b average	92
	4b5p	100
	4b6p	107
	4+b average	104
3 storey houses	3b5p	102
	4b5p	106
	4b6p	113
	4+b average	110

5. Methodology

5.1. Financial Viability Assessments

5.1.1. In line with the National Planning Policy Framework, The London Plan 2011 and local planning guidance as well as the GLA's guidance, 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.

5.1.2. 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.

5.1.3. The RICS define financial appraisals for planning purposes as, 'an objective financial viability test of the ability of a development project to meet its costs including the cost of planning obligations whilst ensuring an appropriate site value for the landowner and a market risk adjusted return to a developer in delivering that project.'

5.1.4. 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.

5.1.5. 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.

5.2. Factors affecting viability

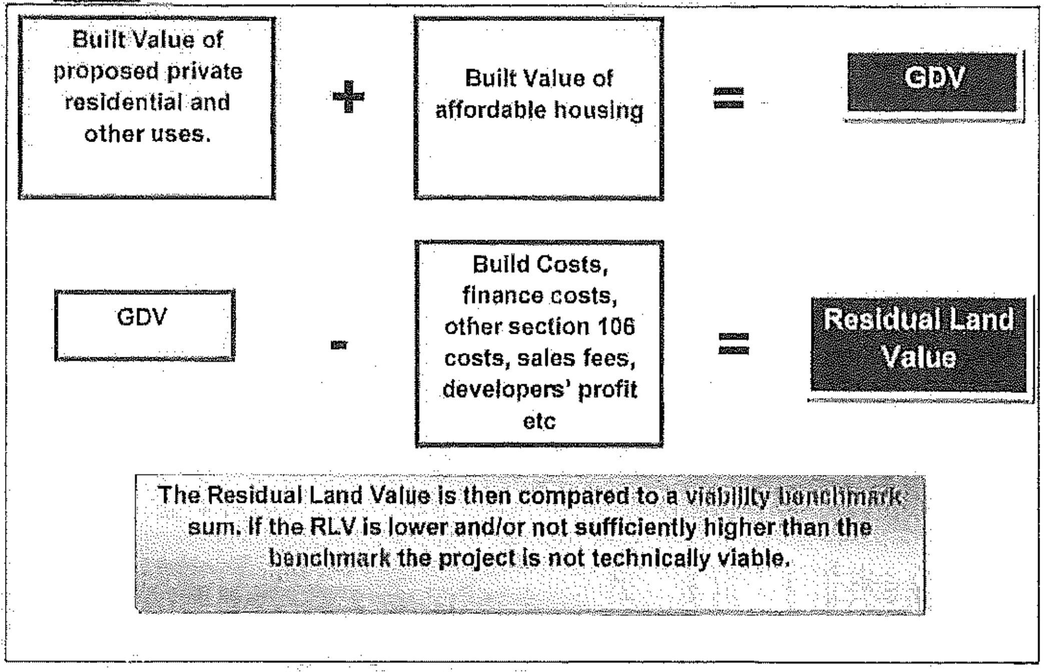
5.2.1. The following factors are particularly relevant to viability:

- Grant funding on the affordable housing;
- The quantity of affordable housing;
- The tenure split within the affordable housing between social/affordable rented and intermediate;
- Cascade clauses related to grant, affordable housing quantum and tenure split;
- Community Infrastructure Levy (CIL);
- 'Other' section 106 costs (e.g. transport, Crossrail etc), or planning gain works;
- Optimum land uses within the development;
- Family sized units;
- Market conditions;
- Timing of delivery/phasing requirements;
- Abnormal building costs;
- Large scale infrastructure requirements; and
- Particular planning requirements.

5.3. Residual Land Valuation

5.3.1. The financial viability of development proposals is determined using the residual land valuation method. A summary of this valuation process can be seen below:

<u>Figure 2</u>



5.4. Developer's Return

5.4.1. The above residual land approach can be inverted so that it becomes a 'developer's return 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 return driven by a scheme.

6. Viability Benchmarks

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. The GLA provides guidance on viability benchmarks for planning purposes and we are also aware that the Royal Institution of Chartered Surveyors (RICS) issued an exposure draft guidance note on 'Financial Viability in Planning' on the 2nd May 2012. Given the available guidance and our own professional experience our views on what constitutes an appropriate viability benchmark are outlined below;

6.1. Existing Use Value/Current Use Value (EUV/CUV)

6.1.1. The EUV, sometimes known as the CUV for Toolkit purposes, refers to the value of the asset at today's date in the adopted planning use. It refers to the Market Value of the asset on the special assumption reflecting the current use of the property only and disregarding any prospect of development other than for continuation/expansion of the current use.

6.1.2. In line with the NPPF we understand that a landowner premium over and above EUV is considered appropriate in order to reflect the fact 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. Having consideration to planning appeal precedents we understand an acceptable level of landowner premium to be at least 15% - 30%.

6.2. Alternative Use Value (AUV)

6.2.1. The AUV refers to the value of the asset under an alternative planning use, either consented or for which permission might reasonably be expected to be obtained.

6.3. Purchase Price Paid

6.3.1. There is much debate about the extent to which purchase price paid (and rolled up debt associated with the site) 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 and reduction in HCA grant funding 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.

6.4. Market Value

6.4.1. The emerging guidance from the RICS contained within their exposure draft 'Financial Viability in Planning' (May 2012) states that when considering the value of the development site for planning purposes the 'Site value should equate to the Market Value subject to the following assumption; that the value has regard to development plan policies and all other material planning considerations and disregards that which is contrary to the development plan.'

6.4.2. The Market Value as defined by the RICS is 'the estimated amount for which the asset should exchange on the valuation date between a willing buyer and a willing seller in an arm's length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

6.4.3. National planning policy states that:

'...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 into 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'.

Para173, National Planning Policy Framework

6.4.4. As such we understand that, in having regard to the development plan the Market Value of a site should reflect a financially viable scheme.

6.5. Developer's Return

6.5.1. As laid out in the RICS guidance 'when a developer's return is the output, a scheme should be considered viable as long as the cost implications of planning obligations are not set at a level at which the developer's return falls below that which is acceptable in the market for the risk in undertaking the development scheme.'

6.5.2. The benchmark return should be at a level reflective of the market at the time of the assessment being undertaken. It will include the risks attached to the specific scheme and also the broader market risk issues such as the strength of the economy and occupational demand, the level of rents and capital values, the level of interest rates and availability of finance. A development project will only be considered economically viable if the estimated developer's return meets or exceeds a benchmark risk-adjusted market sum.

7. Choice of Viability Benchmark

7.1. Existing Site

7.1.1. The Heygate Estate, is a 1970s housing estate owned by Southwark Council, which provides 1,107 residential units within the application boundary, located within several buildings of up to 12 storeys in height. The majority of these apartments are now vacant.

7.1.2. An accommodation schedule of the existing blocks is at **Appendix 5.**

7.2. EUV

Approach to Existing Use Value / Current Use Value

7.2.1. In order to arrive at an EUV/CUV we consider it appropriate to undertake a residual land valuation.

7.2.2. The residual valuation effectively determines the Market Value of the land by deducting all costs including building costs and any profit assumptions from the overall value of the proposed units within the wider scheme ("Gross Development Value") to derive a "balance" available for land purchase.

7.2.3. For the purposes of this appraisal we have assumed that the existing buildings and public realm within the application site have been brought up to a habitable condition in line with Decent Homes and that any commercial space has been refurbished to allow it to be let on the open market. Gardiner and Theobald have undertaken a cost estimate on this basis which is attached at **Appendix 6.**

Unit Mix Assumptions

7.2.4. We understand from SC that there are 1,212 units in total at the Heygate Estate. Of these 1,023 units were under Southwark Council tenancies and 189 were private leasehold units (equating to 15.59%).

7.2.5. We understand that the units are arranged across the Heygate blocks in line with the schedule at para 3.2.3.

7.2.6. In approaching our EUV/CUV, we have pro rated these figures so as to exclude the Wingrave and Rodney Road buildings, which are located outside of the red line plan. This results in 1,107 units in total, of which 934 are to be occupied by affordable tenants and 173 units as private leasehold units.

7.2.7. We have assumed average unit sizes and mix as follows:

Table 5

No. of Units	Type	Tenure	Sqm
89	1b2p	Private	48
60	2b4p	Private	60
16	3b5p	Private	74
8	4p6p	Private	90
478	1b2p	Social Rent	48
327	2b4p	Social Rent	60
88	3b5p	Social Rent	74
41	4p6p	Social Rent	90
1,107 units			**62,542**

GROSS DEVELOPMENT VALUE

Private Market Sales:

7.2.8. In arriving at our opinion of the Market Value for the private units, we have had regard to comparable ex-local authority stock in the area. A brief summary of comparable evidence is included at **Appendix 7**.

7.2.9. We have assumed the following average market values:

- 1 bed 2 person @ 48sq m £170,000 (£329sq ft)
- 2 bed 4 person @ 60sq m £220,000 (£340sq ft)
- 3 bed 5 person @ 74sq m £250,000 (£314sq ft)
- 4 bed 6 person @ 90sq m £280,000 (£289sq ft)

7.2.10. This results in a gross development value of £34,570,000.

7.2.11. We also consider it prudent to assume the following ground rents on the private units, which we have capitalised at a yield of 6%:

- One Bedroom flats: £200pa;
- Two Bedroom flats: £250pa; and
- Three and Four Bedroom flats: £300pa.

Rented Stock:

7.2.12. We have assumed that the 934 units are General Needs Rented (GNR) stock.

7.2.13. GNR is valued on the basis of Existing Use Value Social Housing ("EUV-SH"), which is calculated through an assessment of the net rental income from the properties making allowances for management, maintenance and major repair costs. Rental levels are calculated as Target Rents in line with HCA / TSA Rent Restructuring guidance and on the basis of January 1999 market Values (subject to Vacant Possession). The net cashflow is then discounted back to present day to provide the value of the properties. Key elements of the cashflow are included at **Appendix 8**.

7.2.14. We consider it a reasonable assumption that an Registered Provider would seek to apply full rent caps for each unit type.

7.2.15. Our assumptions in calculating EUV-SH for the GNR units are as follows:

Table 6

Cashflow Input	Assumptions
Average Weekly Rent	£132.59
Real Rent Increases	0.5%
Voids and Bad Debts	2%
Maintenance Per Unit (pa)	£725
Management Per Unit (pa)	£725
Programmed Repair Costs	Years 1 – 10 £0 Years 11 – 15 £200 Years 16 – 20 £600 Years 21 – 25 £800 Years 26 – 30 £800 Years 31 – 35 £1,000
Discount Rate (real)	5.25%
RPI (long term assumption)	2.5%

7.2.16. This results in a total gross EUV – SH of £92m. However, we have deducted "On Costs" of 12% for the social rent units. We have spoken to large number of Registered Providers and these are the typical On Costs they would assume in today's markets. This results in a net EUV-SH of £81m.

7.2.17. The total GDV for the private units and affordable units is therefore circa £115,560,000.

Commercial Space Value

7.2.18. In arriving at indicative values for the existing office and retail commercial space within the application site we have undertaken comparable research into local transactions. A summary of our findings can be seen at **Appendices 9 & 10.**

7.2.19. In addition to the office and retail space we have also had consideration to the existing petrol filling station, garages and doctor's surgery. Given the lack of comparable transactional evidence for space in these uses we have made assumptions based on wider commercial experience.

7.2.20. For clarity, within our appraisal we have assumed:

Table 7

Commercial Element	Annual Rent	Rent Free Period (mths)	Yield
Retail	£13.50 psf	6	8%
Office	£10.00 psf	12	8%
Petrol Filling Station (Assumed Car Showroom)	£13.50 psf	12	8%
Garages	£780 per unit	0	8%
Doctor's Surgery (Assumed Office Space)	£10.00 psf	12	8%

RESIDUAL SITE VALUE

7.2.21. We have assumed a 3 month lead in, 36 month construction period; and an 18 months sales period for the private units.

7.2.22. In coming to our opinion of land value, we have input the figures below into our appraisal (a full summary of the appraisal can be seen at **Appendix 11**):

Table 8

Item	Value
Net Saleable Area – Residential	673,196 sqft
Gross Internal Area – Commercial	39,202sq ft
Total Build Cost (inclusive of contingency)	£57,877,502
Total number of residential units	1,107
Professional Fees @ 6%	£3,028,650
Marketing & Letting	£389,070
Disposal Fees	£830,325
Finance Costs @ 7% debit 1% credit	£5,633,559
Profit on cost @ 16.5%	£17,667,997

7.2.23. This results in a total Existing Use Value of the Site of £37.3m.

7.2.24. We have then applied a 30% landowner premium, which results in a potential benchmark land value of **£48.5m**.

7.3. AUV

7.3.1. For the purposes of this Viability Assessment, we have not given consideration to an Alternative Use Value, but we reserve the right to review this position in the future.

7.4. Purchase Price Paid

7.4.1. A conditional Regeneration Agreement (RA) has been signed by SC and LL for the conditional purchase of the Site.

7.4.2. Under the RA LL are to purchase the Site for £48m plus overage, subject to a number of conditions being satisfied.

7.4.3. The staged land payments for the Site are as follows:

Table 9

Unconditional Date	£5.6m
12 months post Unconditional	£10.7m
24 months post Unconditional	£10.7m
On commencement of 6th Building	£10.0m
On commencement of 7th Building	£5.0m
On commencement of 8th Building	£6.0m
Total	**£48.0m**

7.5. Market Value

7.5.1. We have given consideration to the following unconditional comparable land transactions for sites transacted within LB Southwark from 2010 onwards:

Table 10

Site Address	Size (acres)	Land Price	£ per acre	Date
Elephant and Castle Shopping Centre	3.4	£42,000,000	£12,300,000	18.11.2010
Cantium Retail Park	4.1	£31,000,000	£7,600,000	02.03.2010
254 – 272 Camberwell Road	0.9	£3,000,000	£3,300,000	01.03.2010
Carpetright	1.2	£6,400,000	£5,300,000	31.03.2010

Areas for sites pre-planning have been measured by Molior London (www.moliorlondon.com).

7.5.2. Given the size of the Application Site we have also had consideration to sites sold in the wider south London area over 10 acres;

Table 11

Site Address	Size (acres)	Land Price	£ per acre	Date
Garratt Business Park SW17	15.1	£7,700,000	£500,000	25.03.2011
500 Purley Way CR0	10.4	£34,000,000	£3,300,000	25.06.2010

7.5.3. Further to the above we have also had regard to two large regeneration schemes within Greater London.

Table 12

Site Address	Size (acres)	Land Price	£ per acre	Date
Paddington Basin	16.2	£121,000,000	£7,500,000	October 2011
Earls Court (Council Owned Land)	22	£105,000,000	£4,800,000	Draft Agreement

7.5.4. In addition to our analysis of the transactions outlined above, we have consulted with specialist south east London land agents within the London Residential Development team at Savills L&P. Their view is that given the scale of the Site, likely required infrastructure, prevailing local residential market values, planning designation and anticipated massing, were the Site to be offered to the open market on an unconditional basis it could achieve in the region of £3m to £6m an acre.

7.5.5. Having considered the site comparables above and the view of our specialist colleagues, we have applied a rate of £3m an acre to the Site which results in a Market Value of approximately £72m based on a site area of 9.71 ha (23.98 acres).

7.5.6. Given the EUV/CUV and Market Value detailed above we believe that in this instance Purchase Price is reasonable and as such should be used for the purposes of viability modelling.

7.6. Developer's Return

7.6.1. In assessing what constitutes an acceptable level of developer's return in the current market for the proposed scheme, as well as having regard to our own development experience on mixed use schemes throughout London we have consulted with specialist colleagues within the Loan Security Valuation and Capital Markets departments of Savills.

7.6.2. In order to secure development funding in the current market on a large multi phase scheme we are of the opinion that schemes would need to demonstrate the following developer's return:

Table 13

Planning Status	Profit on Cost	IRR
With Permission	20-25%	15-18%
Without Permission	25-30%	20-25%

7.6.3. Sites without planning permission typically carry a far higher development risk than those with an appropriate and implementable consent. This is reflected above in the higher levels of return required by funders on development sites without planning permission.

7.6.4. Given the status of the Site within adopted local planning policy, as well as the long term Council involvement in this case we would consider that the acceptable level of developer's return would sit at the lower end of the range for sites without planning permission.

7.6.5. As such we would conclude that the viability benchmark position for developer's return in this instance should be 25% profit on cost and 20% IRR.

7.7. Viability Benchmark for The Heygate Estate

7.7.1. In light of the above we are of the opinion that the most appropriate viability benchmark in this instance is **25% profit on cost/20% IRR based on a fixed land value of £48m**.

7.7.2. In addition to the overall viability position achievable by an Illustrative Masterplan, each individual plot must be viable in its own right in order to be implementable.

8. Economic Modelling

8.1. Economic Model Used

The financial analysis has been undertaken using a bespoke financial appraisal (E&C Model 6.24) which appraises the scheme until the end of the projected development period in 2028.

8.2. Economic Modelling Assumptions

The following assumptions have been adopted:

Table 14

Input	Assumption Used
Basic Site Information	User defined number of dwellings.
Choice of Input Method	User defined dwelling types by quantity.
Unit Areas	Floor areas for individual dwellings in the proposed scheme are an average of each type.
Unit Market Values	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 **(Appendix 12)**.
Ground Rents	Ground rents will be charged on the private residential units at an average of £348 per unit per annum. In the Model the ground rents are capitalised at
Parking	The value of the residential parking spaces is included within the private sales value assumed within the Model.
HCA Grant	Since the Comprehensive Spending Review in October 2010 we understand that the HCA will not be supporting the allocation of grant funding to section 106 affordable housing without proving additionality. At this stage no grant funding has been assumed within the Model.
Build Costs	An Initial Indicative High Level Cost Plan has been provided by Gardiner & Theobald **(Appendix 16)**. In addition to this Gardiner & Theobald have also provided advice as to potential overall cost savings **(Appendix 17)**. In light of this advice, the Model incorporates a 2.5% saving upon the costs detailed within **Appendix 16** which reflects the mid point of the potential saving range.

Input	Assumption Used
Escalation Rate	A variable uplift has been applied to both the build costs and capital values over time to reflect price and value movement over the length of the Masterplan. A summary of the Escalation Rates for the different scheme components is provided at **Appendix 18**. The escalation rates for build costs are based upon a consideration of a Cost Trend and Forecast Report (**Appendix 19**) and for residential units are based upon Oxford Economics House Price forecast, **(Appendix 20)**.
Professional Fees	Professional Fees have been included at
Planning Obligations	For the purposes of this viability assessment we have assumed that section 106 contributions of £2,913,160 would be sought by the Council. The Model also includes a £11,683,495 contribution towards Transport for London. A breakdown of the planning contributions is detailed in the draft Heads of Terms at **Appendix 21**.
Community Infrastructure Levy (CIL)	We understand that whilst Mayoral CIL will be payable on the proposal the eligible sum has not yet been determined. As such, the CIL payment is not accounted for in the Model at this moment in time however, the determined figure once incorporated will have a further negative impact on the viability of the scheme.
Interest Rate	The Model assumes an interest rate of

9. Proposed Development Value

9.1. Residential

9.1.1. Private Residential

9.1.1.1. Valuation Method

The private residential proposals have been valued by specialist development consultants in Savills London Residential Development team, using the comparable method of valuation, having regard to the local housing market. Consideration has been given 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.

9.1.1.2. Evidence

The Residential Report prepared by Savills is included at **Appendix 12.**

9.1.1.3. Average Private Residential Values

In summary, Savills report that the comparable evidence supports average values of £500 - £600/sq ft for low rise stock and £650+ for high rise towers.

9.1.1.4. Adopted Private Residential Values

Based on a consideration of the Residential Report and suggested values the Model adopts an average £psf value for each residential block which results in a blended £psf rate for the private residential of **£598 psf**.

9.1.1.5. Car Parking

The values above include revenue from car-parking.

9.1.2. Affordable Residential Values

9.1.2.1. Valuation Method

We have appraised the affordable housing units on a discounted cash flow basis based on the unit breakdown in Table 3 at para 4.2.8, the key elements of the appraisal are included at **Appendix 7.**

9.1.2.2. Evidence

We have regular correspondence with all of the largest Registered Providers (RPs) in the UK, the assumptions adopted within our valuation are based on both general and site specific conversations with those RPs.

For ease we have highlighted the main assumptions used below:

Shared Ownership

- 10% discount on private Market Values;
- Initial Equity Purchase of 25 %;
- Rent on the retained equity varied per unit type in order to comply with Southwark Council's affordability criteria; and
- Appropriate deductions for management and maintenance.

Taking the above assumptions into account this equates to a value of £225psf for the shared ownership units which has been assumed within the Model.

Social Rented

- Rented housing at guideline target rents set through the national rent regime.

Taking the above assumptions into account this equates to a value of £99psf for the social rented units which has been assumed within the Model.

In line with the current HCA Framework we have assumed that no grant will be available on section 106 affordable units without proving additionality.

9.2. Commercial

9.2.1. Overview

The following commercial space is appraised within the Model:

Table 15

Land Use	Use Class	NIA/NSA (m2)
Residential	C3	161,296
Retail	A1/A2/A3/A4/A5	13,198
Business	B1	4,739
Community and Culture	D1	2,410
Leisure	D2	2,048

9.2.2. Office

9.2.2.1. Valuation Method

Farebrother Chartered Surveyors have carried out an appraisal of values for the proposed office space using the comparable method of valuation.

9.2.2.2. Evidence

Comparable evidence prepared by Farebrother is included at **Appendix 13.**

9.2.2.3. B1 Values

As a result of the advice contained within the Farebrother report the following are assumed within the Model:

Table 16

Use	Rent Per Annum £psm (£psf)	Yield
Office		

9.2.3. Retail and Leisure

9.2.3.1. Valuation Method

The retail and leisure spaces have been valued by CBRE, using the comparable method of valuation.

9.2.3.2. **Evidence**

Comparable evidence prepared by CBRE is included at **Appendix 14.**

9.2.3.3. **Retail and Leisure Values**

As a result of the advice contained within the CBRE report the following are assumed within the Model:

Table 17

Use	Rent Per Annum £psm (£psf)	Yield
Retail		
Leisure		
Restaurant		
Showroom		
Supermarket		
Affordable Retail		

10. Viability Results

10.1. Appraisal Results

The results of the development appraisal model 6.24 (**Appendix 22**) demonstrate that the scheme in its current form, incorporating the development costs as laid out in para 8.2 of this report delivers a profit on cost of and an IRR of

When compared to the viability benchmark figures of 25% Profit on Cost and 20% IRR it is evident that the developer's return delivered by an Illustrative Masterplan does not meet or exceed an acceptable risk-adjusted market return and is therefore unviable.

Furthermore when the viability of the individual phases are examined in isolation (Table 19), it becomes even more evident that consideration should be given to ways in which the viability gap might be broached in order to allow the initial phases to be brought forward and the Masterplan delivered.

Table 18

Phase	**Profit on Cost**	**IRR**
Phase 1		
Phase 2		
Phase 3		
Phase 4		
Phase 5		
Phase 6		
Scheme Total		

11. Options Analysis

11.1 As detailed in the previous chapter, the proposed scheme in its current format can not viably sustain the level of planning obligations assumed within the planning application. It therefore follows that in order to ensure viability and enable the development to be deliverable, the level of planning obligations should be considered.

11.2 In order to inform future discussions surrounding the appropriate level of planning obligations for the Site with Southwark Council and the GLA as well as their independent reviewers we would suggest that the following options be considered:

1. Enhancing the value of the proposed affordable housing;
2. Securing grant funding for the scheme;
3. Reducing the financial section 106 obligations; and
4. Reducing the quantum of affordable housing.

11.3 In the first instance, in line with point 1 above, we would advise that the Applicant, in conjunction, with Southwark Council consider the following value enhancement options:

Social Rented

Convert to Affordable Rent at 80% of Market Rent on all rented units.

Convert to Affordable Rent at 80% of Market Rent on the 1 and 2 bed rented units and 65% of Market Rent on the 3+ bed units.

Convert to Affordable Rent at 65% of Market Rent on all rented units.

Convert to Affordable Rent at 65% of Market Rent on the 1 and 2 bed rented units and Target Rent on the 3+ bed units.

Intermediate

All Intermediate housing provided as discount to market sale at 85% of Market Value.

All Intermediate housing provided as discount to market sale at 75% of Market Value.

All Intermediate housing provided as Shared Ownership units compliant with the GLA's adopted policy on affordability thresholds.

All Intermediate housing provided as Shared Ownership units compliant with the mid point between Southwark Council's emerging policy and the GLA's adopted policy on affordability thresholds.

11.4 Once the value enhancements options have been fully examined, should there be a requirement for further redress to the viability gap we would advise that the Applicant seek guidance from Southwark Council and the GLA with respect to points 2-4 above.

12. Conclusions

12.1 In our opinion and based on the economic viability assessment carried out in accordance with the defined guidelines of the Greater London Authority and the emerging guidance from the RICS, it is evident that the scheme cannot afford to provide the proposed level of planning obligations.

12.2 The appraisal model 6.24 indicates that a scheme providing the proposed quantum of affordable housing and wider section 106 contributions drives a developer's return of profit on cost and IRR.

12.3 When compared with the viability benchmarks of 25% profit on cost and 20% IRR, the proposed scheme falls short of being commercially viable, by normal commercial measures of viability.

12.4 The proposals for the Heygate Masterplan represent many years of collaborative work between the Applicant and Southwark Council in order to bring forward this significant regeneration project. Whilst the appraised scheme does not currently work in viability terms, as detailed in chapter 11, there are a number of ways in which we believe the impact of the proposed planning obligations could be mitigated and the viability of the scheme enhanced.

12.5 As such, we would recommend that the value enhancement options are discussed and appraised in order to arrive at a mutually beneficial conclusion.

Appendix 1 – Site Location Plan

Appendix 2 – Scheme Masterplan and Block Drawings

Appendix 3 – Development Specification

Appendix 4 – Proposed Accommodation Schedule

Appendix 5 – Existing Accommodation Schedule

Appendix 6 – G&T Existing Use Refurbishment Costs

Appendix 7 – Existing Private Values Summary

Appendix 8 – Existing Affordable Appraisal

Appendix 9 – Existing Retail Values Summary

Appendix 10 – Existing Office Values Summary

Appendix 11 – EUV Appraisal

Appendix 12 – Savills Proposed Residential Values Report

Appendix 13 – Proposed Affordable Appraisal

Appendix 14 – CBRE Proposed Retail Values Report

Appendix 15 – Farebrother Proposed B1 Office Values Report

Appendix 16 – G&T Proposed Build Cost Estimate

Appendix 17 – G&T Budget Savings Letter

Appendix 18 – Escalation Rates

Appendix 19 – LL Cost Trend & Forecast Report

Appendix 20 – Oxford Economics House Price Report

Appendix 21 – Draft Heads of Terms

Appendix 22 – E&C Financial Appraisal Model 6.24

Provided electronically on the submission CD – NOT available in hard copy.