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Financial Viability Review

On behalf of: Greater London Authority

Bishopsgate Goodsyard

Description:
Review of the Applicant's Financial Viability Assessment, having regard to the due diligence report prepared on behalf of the Local Authorities

CONTAINS CONFIDENTIAL INFORMATION

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March 2016

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EXECUTIVE SUMMARY

1. In order to seek to protect commercially sensitive information, all information issued to us was provided as Commercial-In-Confidence within the meaning of provisions of the Freedom of Information Act, Sections 41 and 43, and the Environmental Information Regulations.

2. Gerald Eve LLP was instructed by the Greater London Authority ("the GLA") to undertake a financial viability review ("the Review") of Bishopsgate Goodsyard ("the Site") and associated information in connection with a planning application, submitted on behalf of a joint venture partnership comprising Hammerson plc and Ballymore Properties ("the JV Applicant"), to London Borough of Hackney ("LBH") and London Borough of Tower Hamlets ("LBTH") for the redevelopment of the Site ("the Scheme").

3. The JV Applicant instructed DS2 LLP ("DS2") to prepare and submit a financial viability assessment ("FVA") which formed part of the planning application documentation. LBH and LBTH instructed BNP Paribas Real Estate ("BNPP") to prepare a due diligence assessment on DS2's FVA, to verify and validate the inputs and reporting on the reasonableness of the S106 (and affordable housing) offer. From what we have reviewed and understand, we are of the view that both practitioners acted independently in order to arrive at their respective differing positions.

4. Negotiations between the JV Applicant and the boroughs were not progressing and the JV Applicant requested that the application be determined by the Mayor of London. The Mayor agreed and the Application was called-in for determination ("the Call-In") by the GLA. The GLA produced their Stage 1 Report on 12th December 2014 and the Stage 2 Report on the 23rd September 2015. Subsequent to the Call-In, the JV Applicant made a revised affordable housing/ S106 offer.

5. We have considered the information and opinions of DS2 and BNPP, and where appropriate we have carried out our own research to help inform our opinions where they differ. We confirm that the viability information and therefore the Review is up-to-date to reflect the market movements, and amendments to the Scheme during the Call-In process. The financial information is therefore correct as at the date of the Review.

6. The Review has regard to the National Planning Policy Framework (the NPPF"), and in particular paragraph's 173-177. We have also had regard to the London Plan Policy

3.12 which states that the maximum reasonable amount of affordable housing should be sought when negotiating on mixed use schemes. Finally, we have had regard to relevant LBH and LBTH planning policies.

7. The Review is in accordance with Planning Practice Guidance (PPG) and Royal Institution of Chartered Surveyors (RICS) Guidance Note: "Financial Viability in Planning" (published August 2012) ("RICS GN 94/12"). The majority of the Review is focused on reviewing the proposed Site Value and appraisal inputs and, other areas we consider must be addressed having regard to PPG and RICS GN 94/12. The Review has also had regard to the GLA Housing SPG of 22 March 2016. We have had an open exchange of correspondence with both DS2 and BNPP, where both consultants have provided us with supporting information where required.

8. We assessed the Scheme on a present day approach reflecting up-to-date cost and value inputs, and also on a growth approach where the developer is in effect forecasting an outcome which has yet to happen and therefore taking all the risk associated with an offer based on that predicted outturn.

9. We have also provided advice on an appropriate viability review mechanism ("the Review Mechanism"). The Review Mechanism enables the Scheme's viability to be monitored to ascertain whether the Scheme is progressing in the manner it was assumed. Any adjustment to affordable housing or planning obligation contribution would need to be justified.

10. The Site Value input was a key area of disagreement between DS2 and BNPP. We are of the view that the DS2 Site Value is more in accordance with the full requirements of PPG and NPPF on viability and therefore the competitive return to the willing seller of land than the suggested more restrictive approach of BNPP. Even after allowances are made for enabling costs, the comparable analysis in our opinion supports the level adopted by DS2. DS2's opinion of Site Value is also consistent with RICS GN 94/12 methods of arriving at a reasonable Site Value.

11. When reviewing the potential level of return across the Scheme, we agree with both consultants that the Internal Rate of Return ("IRR") is the most appropriate proxy to determine the viability of the Scheme.

12. We have assessed the appraisals on two different basis: present day; and growth. Our opinion in relation to an appropriate target rate of return for both are broadly consistent with BNPP, that on a present day basis the target IRR should be 13% to 15% and on a growth basis the target IRR should be a minimum of 20%.

13. The manner in which both consultants have looked to the market to understand current day residential pricing in comparable schemes, which are in the vicinity of the Site, is accepted valuation practice, and encouraged by the RICS. Private residential pricing is one of the key areas of disagreement, whereby the consultants disagree on the comparability of certain local markets and schemes.

14. We are satisfied that the development cost review exercise has been undertaken in an appropriate manned. Whilst there is disagreement in certain areas we consider that the majority of the cost (both construction and infrastructure) input assumptions provided by DS2 are reasonable at this early stage of the delivery process.

15. As a result of our adjustments, our present day appraisal results are shown in the table below.

[redacted]

	[redacted]
	[redacted]
[redacted]	[redacted]

16. In view of the magnitude of the Scheme and the timeframe over which it is to be delivered, it is necessary to consider anticipated future movements in both costs and values to understand the effect of an outturn (growth) approach to viability.

17. In determining appropriate growth rates to apply to residential values and cost inflation, we rely upon data provided by the major property consultancy houses and our own in-house research. A comparative of our two approaches are shown in the table below.

Exec Sum Table 2: Gerald Eve Appraisal Outputs – Present Day and Growth

	[redacted]	[redacted]
	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
TARGET IRR	**14%**	**20%**

18. Whilst a number of the assumptions are agreed, we are of the view that there is likely to be variance in the key variables during the course of the development. We have therefore undertaken sensitivity testing in accordance with best practice, and in considering the robustness of the Scheme appraisal. Variables tested are:-

- Residential sales values
- Construction costs (including utilities, infrastructure and roads).

19. Our analysis is shown in the table below.

[redacted]

[redacted]	[redacted]	[redacted]				
		[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

20. On the basis of the adjustments set out in this report, and the information provided by the JV Applicant, we are of the view the Scheme can afford to provide the maximum reasonable level of affordable housing requirements (25% of affordable housing, by habitable rooms onsite in the LBTH and a PIL of £21,825,000 to the LBH) plus the planning obligations payments of £64m offered.

21. We currently remain of the view that the viability review mechanism within the Convoy's Wharf Section 106 Agreement should form the basis, albeit with certain modifications, and be contained within a S106.

Exec Sum Table 4: Gerald Eve Model: Key inputs and assumptions – Final Offer

Revenue

Residential			
Private	[redacted]	**No. of Units**	[redacted]
Block C	[redacted]	346	[redacted]
Block F	[redacted]	322	[redacted]
Block G	[redacted]	260	[redacted]
Block D	[redacted]	287	[redacted]
Block E	[redacted]		[redacted]
Sub Total	[redacted]	**1,215**	[redacted]
Affordable Rented	[redacted]	**No. of Units**	[redacted]
Block C	[redacted]		[redacted]
Block D			[redacted]
Block E	[redacted]	93	[redacted]
Sub Total	[redacted]	**93**	[redacted]
Intermediate Rented	[redacted]	**No. of Units**	[redacted]
Block C	[redacted]	12	[redacted]
Block D	[redacted]	26	[redacted]
Block E	[redacted]	10	[redacted]
Sub Total	[redacted]	**48**	
Total	**1,082,438**	**1,356**	

Commercial					
Office	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (A) prelet	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (A) cons. letting	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (A) post pc letting	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (B) prelet	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (B) cons. letting	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (B) post pc letting	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Sclater St Cottages Offices (D)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Office (K) prelet	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Offices (K) cons. letting	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (K) post pc letting	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (A) Affordable	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (B) Affordable	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Offices (K) Affordable	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Total	[redacted]				

Retail	**Total NIA Sq ft**	**Rent Psf**	**Yield**	**Void Period (Months)**	**Rent Free Period**
Retail (C)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (H)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (E)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (A)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (B)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (F)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (G)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (L)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (D)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (I)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (J)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Sclater St Cottages Retail (D)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Retail (K)	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
Total	[redacted]				

Other Revenue		
Ground Rent	[redacted]	[redacted]
Block C	[redacted]	[redacted]
Block F	[redacted]	[redacted]
Block G	[redacted]	[redacted]
Block D	[redacted]	[redacted]
Block E	[redacted]	[redacted]
Car Parking	[redacted]	**No. Spaces**

Costs

Borough CIL	**Total Amount**
Site Value	£83,027,728
[redacted]	[redacted]

Type of Construction Costs	Total Amount
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

Additional Development Costs	Total Amount
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

Financial Planning Obligations	Total Amount
Mayoral CIL (LBTH)	£ 4,947,238.00
S106 (LBTH)	£ 2,809,497.00
S106 (LBH)	£ 3,672,041.00
S106 (TfL)	£ 6,500,000.00
Borough CIL (LBH)	£ 15,494,946.00
Mayoral CIL (LBH)	£ 4,950,138.00
Crossrail CIL Top Up (LBH)	£ 4,075,777.00
Hackney Affordable Housing PIL	£ 21,825,000.00
TOTAL	£ 64,274,637.00
Borough CIL	**Total Amount**
Borough CIL (LBH) - Residential	£ 12,466,527.00
Borough CIL (LBH) - Office	£ 2,693,271.00
Borough CIL (LBH) - Retail	£ 335,148.00

Section 106 Contributions Breakdown	S106 (LBTH)	S106 (LBH)	S106 (TfL)
Shoreditch Triangle			£5,900,000
Bethnal Green Road Pedestrian	£250,000		
Travel Plan monitoring*		£12,000	

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Carbon offset payment (site	£837,000	£837,000	
Monitoring fee **	£10,000	£10,000	[£1,500 per Tfl approval]
Cycle docking stations			£600,000
Employment, skills and training ***	£1,162,497	£2,813,041	
[Cycle Improvements]****	£550,000		
*Assuming 3 phases in LBH			
**Currently unknown number of Tfl Approvals	**£2,809,497**	**£3,672,041**	**£6,500,000**
***Subject to justification by LBTH and LBH			
****Subject to justification by LBTH			

[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

Contents

Page

1. Introduction and Instructions 14
2. Background and Description of Scheme 20
3. Planning Policy Overview and Guidance 27
4. Viability Methodology and Approach 38
5. Areas of Agreement 42
6. Review of Value Assumptions and Inputs 44
7. Costs and Construction Programme 54
8. Site Value 64
9. Review of Financial Appraisal 85
10. Growth and inflation 87
11. Sensitivity Analysis 91
12. Review Mechanism 93
13. Conclusions and Recommendations 94

Tables

[redacted]
Exec Sum Table 2: Gerald Eve Appraisal Outputs – Present Day and Growth 6
Exec Sum Table 3: Gerald Eve Growth model IRR sensitivity: residential values and construction costs 6
Exec Sum Table 4: Gerald Eve Model: Key inputs and assumptions – Final Offer 7
Table 5: Summary of Meeting Dates 17
[redacted]
Table 7: Summary areas of Masterplan 25
Table 8: Quantum of uses delivered by Phase 26
Table 9: Areas of agreement 42
Table 10: DS2's private residential pricing assumptions 44
Table 11 BNPP Average Sales Values, July 2015 46
Table 12: Sales Values for Aldgate Place 48
Table 13: Sales Values for The Heron 49
Table 14: Sales Values for Principal Place 50
Table 15: Sales Values for Canaletto 51
Table 16: Construction cost assumptions summary 54
[redacted]
Table 18: DS2's assumed development programme 56
Table 19: Breakdown of Section 106 Obligations – Final Offer 57
Table 20: Detailed Section 106 Financial Obligations 57
[redacted]
Table 22: Summary of Comparable Land Transactions 77
Figure 9: Site Values as a percentage of total GDV 82
Table 23: Site Value Analysis 83
Table 24: Gerald Eve Appraisal Outputs – Present Day 86
Table 25: Adapted from BCIS TPI construction forecasts 88
Table 26: Residential Sale Growth Rates – 88
Table 27: Affordable Housing Growth Rates 89
Table 28: Commercial Growth Assumptions 90
Table 29: Gerald Eve Appraisal Outputs - Growth 90
Table 30: Present day sensitivity: residential values and construction costs 92
Table 31: Growth model sensitivity: residential values and construction costs 92

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Figures

Figure 1: Land Transactions compared against Site - £/ Acre 70

[redacted]

Figure 3: Land transactions compared against Site - £/Unit 72

Figure 4: Land transactions against Site - £/Private Unit 73

Figure 5: Land transactions compared against Site - £/ Acre 78

[redacted]

Figure 7: Land Transactions against Site - £/ Unit 80

Figure 8: Land Transactions against Site - £/ Private Unit 81

Figure 9: Site Values as a percentage of total GDV 82

1. Introduction and Instructions

1.1. Gerald Eve LLP has been instructed by the Greater London Authority ("**the GLA**") to undertake a review ("**the Review**") of the financial viability of Bishopsgate Goodsyard ("**the Site**") and associated information in connection with a planning application, which has been called-in for determination by the Mayor of London ("**Called-In**").

1.2. A planning application was submitted on behalf of Hammerson Plc and Ballymore Properties ("**the JV Applicant**"), to be determined by London Borough of Hackney ("LBH") and London Borough of Tower Hamlets ("**LBTH**") for the redevelopment of the Site ("**the Scheme**")[1].

1.3. The JV Applicant instructed DS2 LLP ("**DS2**") to prepare and submit a Financial Viability Assessment ("**FVA**") which formed part of the planning application documentation. LBH and LBTH instructed BNP Paribas Real Estate ("**BNPP**") to undertake a due diligence exercise on DS2's FVA. All of these documents were made available to us confidentially following our instruction.

1.4. Since the submission of the planning application (August 2014), economic conditions have moved on. We confirm that the viability information and therefore the Review is up-to-date to reflect the market movements, and amendments to the Scheme during the determination period by the boroughs and the Call-In process.

1.5. We have relied upon information supplied which we have interpreted, made assumptions where required and concluded accordingly. Where necessary we have carried out additional research particularly in relation to the Site Value and Sales Values.

[1] During the course of August 2014 to July 2015 the Scheme was amended by the JV Applicant. For the purposes of the Review we have not sought to provide the detail of the changes, as these are dealt with elsewhere. Where we refer to the Scheme, this includes the evolutions to it, from when the original planning application was submitted.

1.6. In accordance with policy and practice (see section 3), we do not seek to compare or contrast the financial offer by the JV Applicant with any other proposed or implemented scheme (or Appeal decision). In accordance with planning legislation, each application should be considered on its own merits. It is also recognised that financial viability, in considering a planning application, is only one of the material considerations as to whether permission should be granted or refused.

1.7. In undertaking the Review we have had regard to national, regional and local policy and guidance. We are formulating an appropriate judgement based upon information provided by the JV Applicant and its consultants, as to the viability of the Scheme and the maximum reasonable level affordable housing and other planning obligations the Scheme can afford.

1.8. Our assessment concentrates on the financial viability of the final offer ("**the Final Offer**") (see paragraph 2.2 and 2.3) having regard to DS2's and BNPP's views and further negotiations with the JV Applicant. Whilst we have not sought to comment on whether it could be improved upon, we provide our views in relation to an appropriate review mechanism ("**the Review Mechanism**") in section 12

Conflict

1.9. So far as we are aware, we have no conflict of interest in relation to the provision of viability advice in respect of this project. We have no on-going or previous fee earning relationship with the JV Applicant, LBH, DS2, BNPP or the Site. We have however worked with DS2 and BNPP on other projects including FVAs.

1.10. We are currently appointed by LBTH in relation to planning and development work on a number of property assets they own or have interests in. We have reviewed the appointment and do not consider it to represent a conflict.

1.11. To confirm when carrying out this review, we have acted objectively, independently and impartially. We consider that DS2 and BNPP have also completed their work in an independent manner.

Inspection of the Site

1.12. In accordance with the acceptance of our instructions, we have viewed the Site and the immediate area.

Confidentiality

1.13. We are aware that in order to seek to protect commercially sensitive information all information issued to us is provided as Commercial-In-Confidence within the meaning of provisions of the Freedom of Information Act, Sections 41 and 43, and Environmental Information Regulations.

Information received

1.14. In undertaking the Review, we have had regard to the following documents:

I. The Goodsyard, Bishopsgate Financial Viability Statement prepared by DS2, dated August 2014 ("**FVA 1**");

II. Review of Financial Viability Assessment prepared by BNPP on behalf of LBH and LBTH, dated July 2015 ("**Due Diligence 1**");

III. The Goodsyard, Bishopsgate Amended Scheme Financial Viability Assessment prepared by DS2, dated July 2015 ("**FVA 2**");

IV. Review of Financial Viability Assessment – Amended Development, prepared by BNPP on behalf of LBH and LBTH, dated November 2015 ("**Due Diligence 2**");

V. Information and documentation in the public domain available through the borough and GLA website:

   a) LBH: Application numbers - 2014/2425
   b) LBTH Application numbers - PA/14/02011
   c) The GLA reference - D&P/1200c&d

Contact with BNPP and DS2

1.15. During the period available to prepare our report we have had an open exchange of correspondence with both DS2 and BNPP, whereby both parties have provided the information requested.

1.16. Both consultants have been supportive in providing us with the information required in order for us to report to the GLA. This has included meetings, email and telephone correspondence.

1.17. The following table provides a summary of the meetings that have been held:

Table 5: Summary of Meeting Dates

Date of Meeting	Location of Meeting	Title of Meeting (if relevant)	Parties Present
22.1.16	GE offices	Viability	GE DS2
5.2.16	GE offices	Viability	GE DS2
5.2.16	GE offices	Due Diligence	GE BNPP
10.02.16	GLA offices	S106 Meeting	GE GLA DS2 JV Applicant
16.02.16	GE Offices	Meeting with DS2: Appraisal run through (technical)	GE DS2
16.02.16	GLA Office	S106 Meeting	ASH GLA DS2/ JV GE
26.02.16	GE Offices	Review Mechanism (technical)	GE DS2
01.03.16	GLA Offices	S106 Meeting	ASH GLA DS2/ JV GE
04.03.16	GE Offices	Meeting with DS2 - Appraisal run through (technical)	GE DS2
10.03.16	GLA Offices	S106 Meeting	ASH GLA DS2 GE/ JV

Source: GE

Our Report Structure

1.18. We set out our report under the following numbered headings:-

Section 2: Background and Description of the Scheme

Section 3: Planning Policy Overview and Guidance

Section 4: Viability Methodology and Approach

Section 5: Areas of Agreement

Section 6: Review of value assumptions and inputs

Section 7: Costs and Construction programme

Section 8: Site Value

Section 9: Review of Financial Appraisal

Section 10: Growth and Inflation

Section 11: Sensitivity Analysis

Section 12: Conclusions

1.19. We set out Sections 4 to 9 under the following sub-headings:

- Summary of information provided;
- Analysis and Comment; and
- Preliminary conclusions.

1.20. We have adopted an approach whereby if we believe the inputs used by DS2 and/or BNPP are within a reasonable margin of our views then we have not sought to challenge these differences. Where these lie outside this margin we have allowed DS2 and the JV Applicant to clarify and comment as necessary. This approach is standard practice and encouraged by PPG, which encourages a collaborative approach between all parties and the RICS in its guidance note for practitioners working in this area, Financial Viability in Planning, published August 2012 ("**GN 94/12**"). We would add that where we have not commented on some aspects of either DS2's reports or BNPP reports and accompanying documents this does not mean we agree or disagree with the consultants, JV Applicant, the Local Authorities or its advisors.

1.21. Finally, it is stressed that this review is taken at a particular point in time (March 2016). Values and costs will change over time and whilst we have had regard to this inevitable uncertainty in the sensitivity analysis section of our report and our concluding recommendations, this report is nevertheless correct as at the time of writing.

1.22. We have had confirmation that DS2 has acted independently and impartially in its preparation and submission of the FVA, and DS2's fee arrangement is not on a contingent basis. In line with Local Authority tendering we understand that BNPP are instructed on a fixed fee basis with no incentives (or contingent fees) with regard to the pending outcome.

1.23. There should be a clear distinction during the viability process between undertaking or reviewing an applicant's viability report and subsequent negotiations, particularly those related to S106 Agreements. Consideration of the viability report should be carried out with objectivity and impartiality.

1.24. Following this viability assessment process, the parties may seek to negotiate acceptable S106 terms. In doing so they may take in to account factors specifically relevant to the applicant. Proposals resulting from these S106 negotiations need to be assessed to ensure they are deliverable both by the applicant and by any third party developer.

1.25. Gerald Eve LLP has reviewed the Applicants financial viability case and the Local Authorities responses. This has been undertaken for the purposes of the Mayors determination.

1.26. Whilst our reporting precedes the signing of the Section 106 Agreement, we have undertaken our report in the shadow of the proposed Heads of the Section 106 Agreement. The detailed negotiations of which will be undertaken at a later stage of the planning process.

2. Background and Description of Scheme

Introduction

2.1. In this section we summarise the background of the S106 negotiations and revised offer to the GLA since submission of the original application to the boroughs. We also comment more generally on the location and description of the Site, with an overview of the Scheme.

Background to final S106 offer to the GLA

2.2. We summarise the S106 negotiations as follows:

I. FVA 1 - DS2 reported that 10% affordable housing (by unit) would be viable in LBH in the form of a payment in lieu ("PiL") of onsite provision. A total of 10% affordable housing (by habitable room) was considered to be the maximum the Scheme could afford in LBTH.

II. [redacted]

III. FVA 2 – DS2 (reflecting an amended scheme) conclude that the equivalent of 10% affordable housing was viable in both boroughs; onsite affordable in LBTH and a PiL of £12m in LBH.

IV. Due Diligence 1 – BNPP of the view that Scheme can viably provide 31% affordable housing onsite in LBTH plus a £12m PiL to LBH (factoring in CIL and Section 106 requirements).

V. September 2015, application Called-In, after which a number of different offers were issued to the GLA and modelled by us. See Table 4 below.

VI. February 2016, the Final Offer is issued, and can be summarised as follows:

A. LBTH to receive 25% affordable housing by habitable room comprising 48 intermediate and 93 social rent

B. LBH to receive a PiL of £21.825 million (which is the equivalent of 15% by dwelling, or 87.3 dwellings split 35 intermediate and 52 social rent)

C. [redacted]

D. Assumptions have also been made on the potential CIL requirements.

E. The GLA have facilitated detailed discussions between the boroughs, Tfl and the JV Applicant to agree an appropriate level of S106 obligations, both financial and non-financial. An offer on these has been finalised.

2.3. As part of our instructions we were asked to review the financial viability of the offers put forward by the JV Applicant. The following table provides a summary of our initial views on viability of the different scenarios.

[redacted]

[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Location and situation

2.4. The Site benefits from excellent accessibility to public transport and has a public transport accessibility level (PTAL) of 6b. Shoreditch High Street station on the London Overground Line is located on Braithwaite Street, within the heart of the Site. It comprises some 4.2 hectares (10.38 acres).

2.5. The Site is partly located in LBH and part within the LBTH. The borough boundary runs in a north south direction to the west of Braithwaite Street.

2.6. The Site has been predominately derelict since a fire in the 1960s and the demolition of the majority of buildings in 2004. In April 2010, Shoreditch High Street Station on the London Overground Line opened in the centre of the Site.

2.7. A number of historic structures occupy the Site and include the Braithwaite Viaduct, the gates, walls and oriel window on the Bishopsgate frontage, all of which are Grade II listed. Also retained on the site are other remnants of the Goodsyard structure, which include the boundary wall on Sclater Street, and the viaduct structures to the south and west of the Braithwaite Viaduct containing coal stores, hydraulic accumulator, rails and a single turntable.

Surrounding Areas

2.8. The area to the north along Bethnal Green Road comprises a mix of former warehouses converted to new uses including residential, small scale industrial estates, shops and the 'Rich Mix' arts and cultural venue.

2.9. To the west is Shoreditch High Street and Old Street which are busy main roads with shops and commercial uses. To the south west is the City of London.

2.10. The area to the south is characterised by a network of smaller streets comprising a mix of residential, commercial and retail uses, extending south towards Spitalfields Market. The eastern edge of the site is defined by Brick Lane, an area characterised by small shops, bars and restaurants with some residential above.

2.11. There are also a number of buildings on the south side of Sclater Street, which lie within the Fournier Street and Brick Lane Conservation Area. These buildings include an unlisted terrace of former weavers' cottages and an unlisted non-conformist chapel.

2.12. The Site is located in close proximity to many designated heritage assets, including listed buildings and conservation areas. A number of conservation areas are located directly adjacent to the Site.

Planning History

2.13. The relevant planning history dates back to 2011. We do not consider that this is significantly material to the outcome of the Review.

The Scheme

2.14. A hybrid application has been submitted for the comprehensive mixed use development of the Site, comprising of outline, full detailed and two separate listed building applications (one in each borough).

2.15. Full details are submitted for plots C, F, G, L and the ground and basement levels of Plots H, I and J.

2.16. The description of development for the planning applications is:

"An outline application for the comprehensive mixed use redevelopment to provide a mixed-use development of the site with all matters reserved for the following uses:

- *Residential (Class C3);*
- *Business Use (Class B1);*
- *Retail, financial and professional services, restaurants and cafes (Class A1, A2 and A3);*
- *Non-residential institutions (Class D1);*
- *Assembly and Leisure (D2);*
- *Public conveniences (sui generis);*

> *Energy centres, storage, car and cycle parking;*
>
> *Formation of a new pedestrian and vehicular access and means of access and circulation of the new site;*
>
> *Provision of new public open space and landscaping.*

Full details are submitted for alterations to and partial removal of existing structures on the site and the erection of three buildings for residential (Class C3) and retail and food and drinks uses (A1, A2, A3, A5); and use of the ground and basement levels of the Braithwaite Viaduct for retail and food and drink uses (A1, A2, A3, A5). Works to and use of the Oriel and adjoining structures for retail and food and drink uses (A1, A2, A3, A5)."

2.17. The Scheme has been informed by a site-wide masterplan concept based on the principles of the Bishopsgate Goodsyard Interim Planning Guidance (2010) ("**the IPG**").

2.18. The Site is divided into a number of 'Building Plots' within which buildings will be developed. Building Plots C, D, E, H, I and J are wholly within LBTH. Plots A, F and L are wholly within LBH. The borough boundary runs between Plots B, G and K.

2.19. The application proposes two landmark tall buildings. Plot F extends to a height of 177.6 m and comprises 46 storeys excluding ground and two rooftop plant storeys. Plot G is lower at 152.4m and comprises 38 storeys excluding ground and two rooftop plant storeys.

2.20. The table below identifies the area assumptions of each plot. The assumptions have been informed by FVA 2, and subsequent revisions in the form of a unit breakdown and distribution of the 25% proposed affordable housing following the JV Applicant's final offer.

GERALDEVE

Table 7: Summary areas of Masterplan

TOTAL						
Private						
		sqm	**sqft**	**sqm**	**sqft**	**units**
	Block C	[redacted]	[redacted]	[redacted]	[redacted]	346
	Block F	[redacted]	[redacted]	[redacted]	[redacted]	322
	Block G	[redacted]	[redacted]	[redacted]	[redacted]	260
	Block D	[redacted]	[redacted]	[redacted]	[redacted]	287
	Block E	[redacted]	[redacted]	[redacted]	[redacted]	0
Sub Total		[redacted]	[redacted]	[redacted]	[redacted]	**1,215**
Affordable Rented						
		sqm	**sqft**	**sqm**	**sqft**	**units**
	Block C					
	Block D					
	Block E	[redacted]	[redacted]	[redacted]	[redacted]	93
Sub Total		[redacted]	[redacted]	[redacted]	[redacted]	**93**
Intermediate						
		sqm	**sqft**	**sqm**	**sqft**	**units**
	Block C	[redacted]	[redacted]	[redacted]	[redacted]	12
	Block D	[redacted]	[redacted]	[redacted]	[redacted]	26
	Block E	[redacted]	[redacted]	[redacted]	[redacted]	10
Sub Total		[redacted]	[redacted]	[redacted]	[redacted]	**48**
Private		[redacted]	[redacted]	[redacted]	[redacted]	1,215
Affordable		[redacted]	[redacted]	[redacted]	[redacted]	141
Affordable Rented		[redacted]	[redacted]	[redacted]	[redacted]	*93*
Intermediate		[redacted]	[redacted]	[redacted]	[redacted]	*48*
Total		[redacted]	[redacted]	[redacted]	[redacted]	**1,356**

Source: DS2 FVA2 and Final offer

2.21. The following table identifies the respective uses which will be delivered in each phase.

Table 8: Quantum of uses delivered by Phase

Phase 1 Uses	[redacted]	[redacted]
Retail	[redacted]	[redacted]
Private Residential	[redacted]	[redacted]
Affordable Residential	[redacted]	[redacted]
Intermediate Residential	[redacted]	[redacted]
Phase 2 Use	[redacted]	[redacted]
Retail	[redacted]	[redacted]
Office	[redacted]	[redacted]
Affordable Office Workspace	[redacted]	[redacted]
Phase 3 Uses	[redacted]	[redacted]
Retail	[redacted]	[redacted]
Private Residential	[redacted]	[redacted]
Phase 4 Uses	[redacted]	[redacted]
Retail	[redacted]	[redacted]
Offices	[redacted]	[redacted]
Private Residential	[redacted]	[redacted]
Affordable Residential	[redacted]	[redacted]
Phase 5 Uses	[redacted]	[redacted]
Retail	[redacted]	[redacted]
Office	[redacted]	[redacted]
Affordable Office Workspace	[redacted]	[redacted]
Overall Summary of Phases		
Retail	[redacted]	[redacted]
Office	[redacted]	[redacted]
Affordable Office Space	[redacted]	[redacted]
Private Residential	[redacted]	[redacted]
Affordable Residential	[redacted]	[redacted]
Intermediate Residential	[redacted]	[redacted]
Overall Total	[redacted]	[redacted]

Source: DS2 and DS2 FVA2

2.22. We understand, so far as the planning application is concerned, that the gross external areas (GEA) identified will not be exceeded in overall terms, but the balance within the latter phases of development may be subject to amendment as detailed design is progressed.

3. Planning Policy Overview and Guidance

Introduction

3.1. In this section we provide a brief overview of our understanding of the policies which set the background and need for viability assessments in order to justify the need for residential accommodation and the level of affordable housing and other planning obligation contributions.

3.2. We provide a high level review of the national, regional and local policies and supporting documents to which the Scheme's affordable housing provision and S106 costs should be considered.

3.3. We also comment upon Scheme specific policy considerations, and refer to RICS GN 94/12.

National Planning Policy Framework

3.4. The NPPF published in March 2012 sets out the Government's economic, environmental and social planning policies for England. It summarises in a single document all previous national planning policy advice. Taken together, these policies articulate the Government's vision of sustainable development, which should be interpreted and applied locally to meet local aspirations.

3.5. In respect of affordable housing, paragraph 50 of the NPPF aims to boost significantly the supply of housing and states that where local planning authorities have identified that affordable housing is needed, they should set policies for meeting this need on site, unless off-site provision or a financial contribution of broadly equivalent value can be robustly justified. Such policies should be sufficiently flexible to take account of changing market conditions over time.

3.6. The NPPF also recognises that development should not be subject to such a scale of obligation and policy burdens that its viability is threatened. This reinforces the need for viability testing in order to allow willing landowners and developers to receive competitive returns which in turn enable the delivery of development.

3.7. The context of achieving sustainable development the NPPF refers to ensuring viability and deliverability at sections 173-177. Section 173 in particular states:

".... To ensure viability, the costs of any requirement 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".

Planning Practice Guidance

3.8. The PPG provides guidance to support the NPPF and to make it more accessible.

3.9. The PPG addresses the question of when and how viability should be assessed by the Council in respect of planning applications. PPG (viability) states:

"....Where the deliverability of the development may be compromised by the scale of planning obligations and other costs, a viability assessment may be necessary. This should be informed by the particular circumstances of the site in question".

A site is viable if the value generated by its development exceeds the costs of developing it and also provides sufficient incentive for the land to come forward and the development to be undertaken."

3.10. The PPG addresses the use of forecast modelling within viability testing as follows:

"Viability assessment in decision-taking should be based on current costs and values. Planning applications should be considered in today's circumstances.

However, where a scheme requires phased delivery over the longer term, changes in the value of development and changes in costs of delivery may be considered. Forecasts, based on relevant market data, should be agreed between the applicant and local planning authority wherever possible."

3.11. With regards to the two boroughs' consideration of planning obligations in relation to viability, including the assessment of affordable housing provision, PPG states:

"In making decisions, the local planning authority will need to understand the impact of planning obligations on the proposal. Where an applicant is able to demonstrate to the satisfaction of the local planning authority that the planning obligation would cause the development to be unviable, the local planning authority should be flexible in seeking planning obligations.

This is particularly relevant for affordable housing contributions which are often the largest single item sought on housing developments. These contributions should not be sought without regard to individual scheme viability. The financial viability of the *individual scheme should be carefully considered in line with the principles in this guidance."*

3.12. PPG defines competitive return for the land owner as:

"The price at which a reasonable land owner would be willing to sell their land for the development. The price will need to provide an incentive for the land owner to sell in comparison with the other options available. Those options may include the current use value of the land or its value for a realistic alternative use that complies with planning policy." (Paragraph 24)

3.13. PPG refers to three strands, all of which should be considered:

"The most appropriate way to assess land or site value will vary from case to case [but] In all cases, land or site value should:

- *reflect policy requirements and planning obligations and, where applicable, any Community Infrastructure Levy charge;*
- *provide a competitive return to willing developers and land owners; and*
- *be informed by comparable, market-based evidence wherever possible. Where transacted bids are significantly above the market norm, they should not be used as part of this exercise"*

The London Plan (March 2015) incorporating the Further Alterations to the London Plan (2015) and the Minor Alterations to the London Plan (March 2016), and GLA Supplementary Housing Planning Guidance (March 2016)

3.14. On 10 March 2015, the Mayor adopted the Further Alterations to the London Plan ("**FALP**"). From this date, the FALP are operative as formal alterations to the London Plan. On the 14 March 2016, the Mayor adopted the Minor Alterations to the London Plan ("**MALP**"). From this date, the MALP are operative as formal alterations to the London Plan.

3.15. On the 22 March 2016, the Mayor adopted the Housing Supplementary Guidance ("**Housing SPG**"). This was updated to reflect the FALP and the MALP. It replaces the 2012 Housing SPG and the Mayors Housing Standards Policy Transition Statement.

3.16. The London Plan builds upon many of the policies set out at the national level with a significant emphasis upon achieving development in the most suitable and sustainable of locations, prioritising the use of previously developed land and making the most efficient use of available land.

3.17. The London Plan establishes the need for regional growth in housing and employment and identifies further development in the Central Activities Zone ("**CAZ**") and associated Opportunity Areas as a means by which this requirement can be accommodated. The London Plan seeks that development should maximise the potential of sites, create or enhance the public realm, provide or enhance a mix of uses, respect local context, character and communities and be sustainable.

3.18. Policy 2.11 of the London Plan encourages a range of uses within the CAZ and states that where a development proposes an increase in office floor space, proposals should include a mix of uses including housing. Policies 2.10 and 2.11 of the London Plan also seek to support and improve the retail offer of the CAZ residents, workers and visitors.

3.19. Policy 2.13 identifies the need to "encourage rather than restrain" development and "promote mixed and balanced communities" having regard to the need, size and type of affordable housing required, as well as the specific circumstances of the site.

3.20. Similarly, Policy 3.8 states, that whilst boroughs should seek the maximum reasonable amount of affordable housing, regard should be had to the need to encourage rather than restrain residential development. Negotiations on sites should take account of their individual circumstances, including development viability.

3.21. Policy 3.10 goes on to state that affordable housing including social rented and intermediate housing, should be provided to meet the needs of specific households whose needs are not met by the market.

3.22. Policy 3.11 sets out the affordable housing targets for London. The London Plan now seeks a preferred tenure split of 60% social rented and 40% intermediate housing and priority should be given to provision of affordable family housing.

3.23. Policy 3.12 states that the maximum reasonable amount of affordable housing should be sought when negotiating on residential schemes. In particular the policy sets out that regard should be had to the current and future requirements for affordable housing at local and regional levels. Going on to state that there is a need to encourage rather than restrain residential development and promote mixed and balanced communities.

3.24. London Plan Policy 3.8 encourages a full range of housing choice. This is supported by the SPG which seeks to secure family accommodation.

3.25. SPG section 4 provides guidance on the recommended approach to consideration of FVA. This re-iterates the approach recommended in NPPF and in para 4.1.4 states:

"... In light of inference to the contrary...either 'Market Value', 'Alternative Use Value', 'Existing Use Value plus' based approaches can address this requirement where correctly applied (see below); their appropriate application depends on specific circumstances."

The London Plan and SPG Housing: Review Mechanisms

3.1. The London Plan refers to the use of S106 agreements to enable and define mechanisms for the re-appraisal of viability prior to the implementation of schemes in whole or in part which are likely to take years to implement.

3.2. Policy 3.12 states that the negotiation of affordable housing should include *"provisions for re-appraising the viability of schemes prior to implementation".*

3.3. In the Housing SPG, clause 4.3.3 states that review mechanisms are encourages to be considered when a large scheme is built out in phases and/or is built out over a long period of time.

3.4. Clause 4.3.5 then confirms the need for boroughs to ensure the following when establishing review mechanisms:

- *Identity the point(s) at which the appraisal should be carried out;*
- *Establish on a case-by-case basis the threshold level(s) of viability at which additional planning obligation contributions will be required;*
- *Establish what the review will assess: for example some reviews assess all aspects of a development appraisal, while others are limited to changes in gross development value (GDV) or GDV and build costs;*
- *Establish if the review 'looks back' i.e. calculates additional contributions based on the completed phase or if the review 'looks forward' and uses the information from the completed phase to inform the requirements of the next phase;*
- *Set a 'cap' on the additional provision that will be sought based on ensuring policy compliance;*
- *Agree the profit split between the developer and borough once the threshold level of viability has been reached;*
- *Set out the requirement for additional home on or off site or for receiving a financial contribution.*

The London Plan: City Fringe Opportunity Area

3.5. The Site is located within the City Fringe Opportunity Area ("**CFOA**") designated within the London Plan. Policy 2.3 states that development proposals within such areas should:

- Support the strategic policy directions for Opportunity Areas;
- Seek to optimise residential and non-residential densities and where appropriate contain a mix of uses;

- Contribute towards meeting (or where appropriate, exceeding) the minimum guidelines for housing and/ or employment capacity; and
- Support wider regeneration (including in particular improvements to environmental quality) and integrate development proposals to the surrounding areas especially areas for regeneration.

3.6. The CFOA is identified in the London Plan (2015) as an area for significant growth over the next 20 years with a target of a minimum of 8,700 new homes and 70,000 new jobs by 2031. The Mayor of London's '2020 Vision' (July 2013) refers to the Site directly as a key area for future delivery of housing and employment.

Bishopsgate Goodsyard Interim Planning Guidance (2010)

3.7. The IPG was prepared and adopted as planning guidance by the LBH and LBTH and forms part of the Local Development Framework for both boroughs and approved by the GLA.

3.8. The IPG sets out that the regeneration of the site should provide a mix of uses, comprising tall buildings and public open space.

3.9. The IPG recognises that the development should provide a mix of housing tenures, including market sale, intermediate and social rented housing to meet local needs. It states that a minimum of 35% affordable housing should be provided onsite subject to viability and site circumstances outlined in the London Plan.

Local Policies

3.10. At the local level, the Site is also identified as 'Site Allocation 1 (SA1)' within the LBTH Managing Development Document ("**MDD**") and 'Site Allocation 108' in the LBH Site Allocations Local Plan. Both developments mirror the IPG and identify the Site for a comprehensive mixed-use development.

London Borough of Hackney

3.11. LBH Core Strategy was formally adopted in 2010. This was followed by the Proposed

Development Management Local Plan in 2013.

3.12. Core Strategy Policy 3 advises that: "The council will balance the objectives of economic development with protection and enhancement of the local architectural and historic character.

Core Strategy Policy 20

- LBH has a Borough-wide affordable housing target of 50% of all units subject to site characteristics, location and overall scheme viability.
- Affordable housing will be sought on all developments comprising 10 or more units
- In line with identified need and as a borough wide guide the required tenure split of affordable housing will be 60% social rented and 40% Intermediate (by unit). On individual sites the exact tenure split will be guided by up to date assessments of specific local housing need and site and neighbourhood characteristics.
- For all new social rented and intermediate homes, the preferred affordable housing size mix will include an element of 3 bed or larger family housing in line with or exceeding the minimum requirement set out in the London Plan and addressing specific priority housing need in Hackney.
- The preferred affordable housing mix, in terms of unit size and type of dwellings, on individual schemes will be determined through negotiation, scheme viability assessments and driven by up to date assessments of local housing need.
- The Council has a preference for on-site delivery of affordable housing, but where it can be demonstrated that on-site provisions is not practical or viable, off site provision within the vicinity and then elsewhere in the Borough will be considered. In circumstances where all of the cascade options have been explored and proven impractical or unfeasible, a payment in lieu ("**PiL**") will be acceptable.

London Borough of Tower Hamlets

3.13. The LBTH Core Strategy was adopted in 2010, followed by its MDD in April 2013.

3.14. Core Strategy SP02 sets overall strategic target for affordable homes:

- 50% until 2025. This will be achieved by requiring 35%-50% affordable homes on sites providing 10 new residential units or more (subject to viability);
- Require an overall strategic tenure split for affordable homes from new development as 70% social rented and 30% intermediate;
- Secure a mixture of small and large housing by seeking a mix of housing sizes on all sites providing new housing requiring an overall target of 30% of all new housing to be of a size suitable for families (three-bed plus), including 45% of new social rented homes to be for families.

3.15. DMP3 states the following:

- Development will be required to maximise affordable housing in accordance with the Council's tenure split (70% Social/Affordable Rent and 30% Intermediate) as set out in the Core Strategy;
- Affordable housing should be built to the same standards and should share the same level of amenities as private housing;
- Development should maximise the delivery of affordable housing on-site;
- Any off-site affordable housing will only be considered in specific circumstances.

The RICS Guidance Note: Financial Viability in Planning

3.16. GN 94/12 was published in August 2012, after the NPPF. The purpose of the guidance note is to enable all participants in the planning process to have a more objective and transparent basis for understanding and evaluating financial viability in a planning context. It provides practitioners with advice in undertaking and assessing viability appraisals for planning purposes.

3.17. The GN 94/12 defines financial viability for planning purposes; separates the key functions of development, being land delivery and viable development (in accordance, and consistent, with the NPPF); highlights the residual appraisal methodology; defines Site Value for both scheme specific and area-wide testing in a market rather than hypothetical context; what to include in viability assessments; terminology and suggested protocols; and the uses of financial viability assessments in planning.

3.18. The guidance note provides all those involved in financial viability in planning and related matters with an objective methodology framework and set of principles that can be applied for both plan making and development management.

3.19. The guidance note is grounded in the statutory and regulatory planning regime that currently operates in the UK. It is consistent with the Localism Act 2011, the NPPF and the Community Infrastructure Levy ("CIL") Regulations 2010 (as amended).

3.20. Financial viability for planning purposes is defined as follows:-

"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 the developer in delivering that project."

3.21. The RICS GN 94/12. addresses "competitive return" as follows:

"A term used in paragraph 173 of the NPPF and applied to 'a willing land owner and willing developer to enable development to be deliverable'. A 'Competitive Return' in the context of land and/or premises equates to the Site Value as defined by this guidance, i.e. 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. A 'Competitive Return' in the context of a developer bringing forward development should be in accordance with a 'market risk adjusted return' to the developer, as defined in this guidance, in viably delivering a project. ."

3.22. The NPPF has a clear presumption in favour of sustainable development and in determining planning applications local authorities should take account of this.

3.23. The NPPF recognises that development should not be subject to such a scale of obligation and policy burdens that its viability is threatened; and in addition, obligations should be flexible to market changes in order to ensure planned development are not stalled. This reinforces the need for viability testing in order to allow willing landowners and developers to receive competitive returns which in turn enable the delivery of development.

3.24. Under the local policies the boroughs seek the maximum provision of affordable housing with a strategic target for 50% affordable housing from all sources.

3.25. Under the London Plan, Policy 3.12 outlines the ability to negotiate the level of affordable housing on individual private residential and mixed use schemes. It states that the maximum reasonable amount of affordable housing should be sought when negotiating on mixed use schemes.

3.26. The PPG and best practice guidance such as RICS GN 94/12 recognises the need for FVAs which accompany planning applications to be determined, should be up to date and relevant.

3.27. The London Plan and Housing SPG identify the need to establish a review mechanism for large and complex schemes that are set to be delivered over a long period of time. It is important that when designing the mechanism, regard is given to both documents.

4. Viability Methodology and Approach

Introduction

4.1 In this section we review DS2's methodology and approach in assessing viability. We also have regard to the BNPP due diligence reports.

Summary of information provided

4.2 <u>Viability Appraisal</u>: Both DS2 and BNPP have undertaken their appraisals of the Scheme using Argus Developer software. Both have used residual appraisal methodology to assess the Scheme's viability.

4.3 <u>Site Value</u>: DS2 has adopted an overall Site Value of £83,027,280 through the use and analysis of land transactions considered comparable. BNPP has proposed a benchmark land value of £20m based on their opinion of an historic Existing Use Value ("**EUV**"), which has been inflated.

4.4 <u>Residential and commercial values</u>: DS2 has used comparable sales, rental and investment evidence to aid in the justification of value to the Scheme. BNPP has provided further evidence which it considers comparable and relevant.

4.5 <u>Build costs</u>: DS2 has relied upon construction costs provided by Gardiner & Theobald ("**G&T**"). The boroughs originally sought independent advice from Synergy LLP on costs, and then WT Partnership ("**WTP**").

4.6 <u>Development programme</u>: DS2 has assumed different programmes for its FVA 1 and FVA 2. BNPP questioned the duration of the programme assumption originally put forward by DS2 and the JV Applicant. DS2 provided further justification of the assumed phasing during the call-in, subsequent to our requests.

4.7 <u>Basis of assessment</u>: DS2 has undertaken its appraisal on a present day basis and sought to introduce growth once appraisal variables were at an agreed stage with BNPP.

4.8 <u>Consultancy fees</u>: DS2 has made standard industry assumptions in relation to agents, marketing, legal and professional fees.

4.9 **Affordable housing, S106 & CIL costs**: The JV Applicant and DS2 consider the final offer to be the maximum reasonable level of affordable housing, S106 and CIL that can be provided.

4.10 **Developer return**: Both consultants agree that the IRR is the most appropriate measure of viability. DS2 considers an appropriate target return for the Scheme to be 20% on a present day approach and 25% assuming a growth approach. BNPP consider an appropriate range for a present day approach should be between 12% and 14%.

4.11 **Sensitivity analysis**: Sensitivity analyses do not form part of either viability consultants reporting.

Analysis and Comment

4.12 Negotiations between the JV Applicant and boroughs have been ongoing since 2014.

4.13 **Agreement on residual approach**: The consultants agree that the residual methodology is the appropriate way to assess the viability of the Scheme. We agree with the approach, and add that this is consistent with GN 94/12, being the recognised way of assessing for viability for planning purposes. We have prepared a bespoke model on Microsoft Excel.

4.14 **Disagreement on Site Value**: We comment further on this in section 8.

4.15 **Disagreement on sales values**: We comment further on this in section 6.

4.16 **Build Costs**: We comment further on costs in section 7.

4.17 **Sensitivity analysis and growth**: Assessing the Scheme on a present day basis provides a base position upon which the inevitable uncertainty of the development process can be measured. We comment further on this in section 11.

4.18 **Use of review mechanism**: Where appropriate, the approach of including a review mechanism prior to the implementation of any future phase can be an acceptable approach in meeting the "maximum reasonable" criteria in respect of affordable housing (and planning obligations). Any adjustment to affordable housing or planning obligation contribution would have a cap, being the maximum planning requirements contribution, and collar, which is the level of planning requirement provision below which the development would be unacceptable. We comment further on this in section 12.

4.19 **Return proxy**: Given the length of the development programme, and the phased delivery profile we are of the view that measuring the Scheme on the basis of an IRR is a good representation for the viability for the Scheme. Importantly the IRR takes into consideration the time value of money.

4.20 **Appropriate target for developer's competitive return**: We consider the minimum target rate of return on a growth basis to be an IRR of 20% which is risk adjusted relative to the following characteristics:-

I. Site complexity/ constrained nature/ neighbouring buildings/ substructure works needed;

II. The length of the proposed construction period;

III. The proposed residential sales assumptions and speculative construction of a large proportion of the site;

IV. The uncertainty surrounding the letting of the commercial elements;

V. The capital intensive nature of the phased development programme;

VI. The uncertainty over the Scheme to achieve the residential pricing levels;

VII. Growth modelling with assumptions made in respect of values and costs and likely outturn;

VIII. By comparison with other key strategic sites we have directly worked upon.

Preliminary Conclusions

4.21 We agree that residual methodology should be used to test the viability of the Scheme for planning purposes. Both consultants have broadly followed GN 94/12 in their approaches. This is the approach we have used to test the final offer put forward by the DS2 and the JV Applicant.

4.22 We do not consider that BNPP's approach in assessing the benchmark land value, or Site Value[2], is consistent with PPG or the NPPF. Because of the specific factors affecting this site, the assessment of an EUV of the Site, which has been inflated, does not, in our view, meet the national policy and guidance provisions set out in paragraphs 3.7, 3.13, and 3.14 above. With regard to DS2's assessment of Site Value, there have been areas we have sought clarification on. Having undertaken further due diligence

[2] As defined in RICS GN 94/12

(which we provide commentary on below in section 8), we are of the view that DS2 has met the policy provisions of the NPPF and PPG in its assessment of Site Value. Its assessment is broadly consistent with best practice guidance.

4.23 In order for us to report in a robust manner we consider that the Scheme should not only be assessed on a present day basis but also having regard to growth. Growth modelling with a suitable review mechanism, is necessary to making sure the Scheme delivers the maximum reasonable provision of affordable housing.

4.24 Modelling the output upside and downside should, to varying degrees, be reflected in a sensitivity analysis. This provides the certainty that, whilst a developer may not be reaching his target rate of return, the Scheme is potentially capable of reaching it having regard to movements in key variables.

4.25 The most appropriate return proxy for this is approach is to assess the Scheme against a market adjusted target IRR.

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5. Areas of Agreement

Introduction

5.1 In this section we provide a summary of agreed matters between the two consultants. We then provide our opinion where necessary.

Summary of information provided

5.2 The table below summarises areas of agreement.

Table 9: Areas of agreement

Element	Appraisal Input
Total Residential Units	1,356 total units
Scheme Areas	
Total Residential	[redacted]
Private Residential	[redacted]
Affordable Rent Residential	[redacted]
Intermediate Residential	[redacted]
Retail Areas	[redacted]
Office Areas	[redacted]
Revenue	
Average Retail Values	[redacted]
Average Office Values	[redacted]
Ground rent income:	[redacted]
Programme	**Block** **Start** **Duration** **End** Block C Jul-16 48 Jul-20 Block E Jul-16 48 Jul-20 Block F Jul-21 42 Jan-25 Block G Jul-21 42 Jan-25 Block D Oct-24 63 Jan-30
Costs	
Additional Acquisition Costs	[redacted]
Residential Marketing	[redacted]
Commercial Disposal Agents Fees	[redacted]
Residential Sales Legal Fee	[redacted]

Finance:	[redacted]

Analysis and comment

5.3 So far as the information in Table 9 is concerned, we comment as follows:

I. Floor Areas: Within the final offer, the affordable housing element has been calculated based on 25% (by habitable rooms) onsite, located in blocks C, D and E in LBTH.

II. Programme: During the review process we asked the JV Applicant to provide a more detailed justification for the overall development programme and the length of individual phases within this.

III. Where we have not commented, we are broadly in agreement with both consultants.

Preliminary Conclusions

5.4 A number of the assumptions put forward by the respective consultants have been agreed. Given the early nature of where the JV Applicant is in the development process we are of the view that there is likely still to be variance in these.

5.5 Notwithstanding the variance, the inputs are considered to be reasonable for the purposes of assessing financial viability in planning.

6. Review of Value Assumptions and Inputs

Introduction

6.1. In this and the following section we review the inputs relating to residential values and sales velocity. We provide a summary overview of the consultants' inputs, then review the source of each element, and finally provide comment and analysis. We also have regard to the need to update the appraisal to current day market conditions.

Summary of Information Provided

Private Residential - DS2

6.2. [redacted]

6.3. [redacted].

Table 10: DS2's private residential pricing assumptions

Phase	Type and block	[redacted]	Location	Other uses
1	PR – Block C	[redacted]	LBTH	Intermediate Housing Retail
	PR – Block E	[redacted]	LBTH	Affordable Housing
3	PR – Block F	[redacted]	LBH	Retail
	PR – Block G	[redacted]	LBH	Retail
4	PR – Block D	[redacted]	LBTH	Retail Affordable Housing
	Average Psf	[redacted]		

6.4. DS2 has based its residential sales values on comparable evidence obtained from the Molior Database ("**Molior**"), London Residential Research and a number of other property research websites that are not referenced.

6.5. DS2 consider their evidence has been selected based on the following criteria:

- Competing new and modern tower apartments in the vicinity;
- Schemes that are coming forward but do not yet have marketing and sales information available;

- Towers located further afield that are in excess of 40 storeys which can be used to establish the values for Blocks F and G.

6.6. DS2 has provided the following comparables as justification for its inputs:

- St George Wharf – The Tower, Vauxhall
- Baltimore Wharf, Canary Wharf
- Principal Tower, North end of Bishopsgate
- Providence Tower, Canary Wharf
- Saffron Square, Croydon
- One Blackfriars, Bankside
- 250 City Road, Islington
- Eileen House, Bankside
- Morello Tower, Croydon
- South Bank Tower, Bankside
- One Nine Elms, Wandsworth

6.7. [redacted]

6.8. A unit by unit breakdown for Blocks C, F and G was provided. As Blocks D and E are in outline, a detailed schedule is not available and broad assumptions made. An independent sales report from a residential sales agent was not provided.

6.9. [redacted]

Private Residential - BNPP

6.10. BNPP comment that the schemes which are the most relevant and updated to the site include:

- Principal Place;
- 1 Crown Place

6.11. BNPP also comment upon the overall changes in residential values in both of the boroughs during the period from July 2012 to September 2015. They specifically refer to the 'Land Registry House Price Index' for the same period.

6.12. BNPP include a pricing schedule detailing the proposed anticipated sales values for the each block within the scheme, but provide no rationale for the pricing assumptions.

Table 11 BNPP Average Sales Values, July 2015

Phase	Type and block	[redacted]	Location
1	Block C	[redacted]	LBTH
	Block E	[redacted]	LBTH
3	Block F	[redacted]	LBH
	Block G	[redacted]	LBH
4	Block D	[redacted]	LBTH
	[redacted]	[redacted]	

6.13. [redacted]

Affordable Residential – DS2

6.14. [redacted]

6.15. [redacted]

Affordable Residential – BNPP

6.16. [redacted]

6.17. [redacted]

6.18. BNPP have not commented on the timing of the affordable housing revenue.

6.19. BNNP have not provided a breakdown of the potential affordable housing values according to block or location within the scheme.

Commercial Values

6.20. We set above in **Table 9**, in section 5 the areas of agreement between the respective viability consultants. Clearly there is a considerable amount of agreement between the professionals in relation to the commercial value inputs.

6.21. We have undertaken a high level review of these commercial value inputs, and are in broad agreement with both DS2 and BNPP. We are not therefore seeking to comment in greater detail, as the inputs are considered to be within a reasonable range given current market conditions.

6.22. We have looked in detail at the sales assumptions associated with the disposal of commercial elements, and we are the view that a reasonable exit assumption would be at the end of the void period. [redacted]

Analysis and Comment

6.23. Generally, we appreciate that the market for flats in high rise towers is different to those in low rise. There is recognition of quantitative increases of in the value of the units the higher the unit is in a tower. The analysis from both DS2 and BNPP should have been broken down between different block types and property sizes, and with further comment on price variations depending on floor levels in high rise towers.

6.24. Where information has been available in relation to actual completed sales values, we have used these to benchmark our views from, rather than quoting prices. DS2 has provided further information in relation to sales. Generally speaking we are of the view that DS2 and BNPP have assessed values on a broad basis. This allows for considerable variance in residential values, which is considered to be the major value driver of the Scheme.

6.25. In order to fully assess the evidence presented by both consultants, we have completed a review of surrounding schemes.

6.26. Key comparables identified by BNPP (Principal Place and 1 Crown place) are based on early pricing and asking pricing. Through our research we know that some sales have been achieved to date.

Aldgate Place, 10 Whitechapel High Street, E1

6.27. This scheme is a mixed use development comprising three towers of 22, 25 and 26 storeys. It also includes a series of lower level buildings ranging from six to nine storeys, and is located close to the Site.

6.28. We understand it will provide 463 residential units of which 151 are affordable.

Table 12: Sales Values for Aldgate Place

.	Max	Avg	Min
Price:	£1,155,000	£916,885	£665,000
£psf	£1,441	£1,198	£834
Sq. ft	1,247	786	538

	Max	Avg	Min
Studio:	£0	£0	£0
1 Bedroom	£775,00	£744,000	£665,000
2 Bedroom	£1,035,000	£921,750	£780,000
3 Bedroom	£1,155,000	£1,042,885	£971,000

Source: Molior, February 2016

6.29. We understand that an average rate of £1,262 psf was achieved for sales that took place in Q3 of 2015. These ranged from £1,170psf for a one-bed, £1,253 psf for a two-bed to £1,435psf for a three-bed.

6.30. Aldgate Place is in an inferior location. The site is further away from the City, located on a busy high street and does not have the benefit of the public park. Pricing here is likely to be at the lower end of what we consider could be achieved at the Site. The blended average for the Scheme would, in our view, be significantly higher

The Heron, EC2Y,

6.31. The site is located within the City of London. It provides a total of 284 residential units with no affordable housing. Construction of the site completed in the summer of 2013.

6.32. The following table summarises the asking prices for the scheme, as of February 2016.

Table 13: Sales Values for The Heron

	Max	Avg	Min
Price:	£15,000,000	£1,144,171	£415,000
£psf	£2,549	£1,341	£885
Sq. ft	6,077	743	398

	Max	Avg	Min
Studio:	£705,000	£532,429	£415,000
1 Bedroom	£925,000	£734,407	£499,000
2 Bedroom	£3,800,000	£1,471,958	£799,000
3 Bedroom	£10,000,000	£3,466,429	£1,260,000

Source: Molior, February 2016

6.33. We understand that from June 2015 to early 2016, a total of four sales took place in the building. The units were all Studios and 1 beds, with 3 located below the 20th floor. An average rate of £1,500 psf was achieved across sales, ranging from £1,356 psf to £1,611 psf.

6.34. The Heron is in the City location, and whilst the units may appeal to a slightly different market to that of the Scheme, there are similar characteristics given the high rise nature of the building. The Scheme units are unlikely to achieve the top end of prices paid at the Heron (in today's conditions). We are of the view that the blended rate across the Scheme will not reach those of the Heron, [redacted]

Crown Place, EC2M

6.35. The scheme includes two towers of 29 and 33 storeys as well as office, retail and hotel accommodation. Planning permission was achieved in June 2015, and it will provide a total of 247 private units. The location and composition of this scheme is considered to be comparable to the Site and the Scheme. Crown Place does not provide affordable housing.

6.36. BNPP report that the scheme has average asking prices of £1,500 psf although we are unable to verify this due to a lack of information provided by the Agents of the scheme.

Principal Place, Worship Street, Hackney, E1 6PJ

6.37. This development comprises a 50 storey block, of which one part is 10 and one part is 16 storeys, a 14 storey block and one 6 storey block. A total of 243 private residential and 56 affordable units will be provided with retail and office space.

6.38. This scheme is considered comparable as it is located in close proximity to the Site and includes a range of different block sizes, including one of 50 storeys. It also will provide c.25% affordable housing.

Table 14: Sales Values for Principal Place

.	Max	Avg	Min
Price:	£4,800,000	£1,856,407	£794,000
£psf	£2,330	£1,804	£1,439
Sq. ft	2,179	1,003	453

	Max	Avg	Min
Studio:			
1 Bedroom	£1,339,00	£1,146,000	£794,000
2 Bedroom	£3,019,00	£2,113,103	£1,328,000
3 Bedroom	£4,800,00	£4,725,000	£4,650,000

Source: Molior (February 2016)

6.39. The above data, whilst stated to be asking, does in our view provide a strong indication of where the local market currently is. Reasonable downward adjustments to the above data would suggest that improvements in value to the Scheme can be justified.

Canaletto, City Road EC1V

6.40. This development comprises a 31 storey block plus basement; a total of 190 private residential and 56 affordable units; landscaping and public realm improvements. The scheme is considered to be comparable because of its locational and design/massing characteristics.

6.41. We understand that a total of 182 units are now complete and a further eight are due to be completed by the end of Q1 2016. At the end of Q3 2015 eight units remained unreleased and three units available. Construction is expected to complete by the end of Q1 2016.

Table 15: Sales Values for Canaletto

.	Max	Avg	Min
Price:	£3,300,000	£1,294,327	£500,000
£psf	£1,722	£1,303	£970
Sq. ft	1,991	963	388

	Max	Avg	Min
Studio:	£520,000	£510,000	£500,000
1 Bedroom	£950,000	£840,000	£720,000
2 Bedroom	£1,365,000	£1,125,857	£835,000
3 Bedroom	£3,300,000	£2,625,000	£1,825,000

Source: Molior (February 2016)

6.42. The values above are reported to be asking prices, not actual sales. On research, we understand that only limited information on sale prices has been released.

6.43. Based on the information that has been provided, we understand that between March and October 2015, an average sales rate of £1,475 psf was achieved. This ranged from £1,431 for a one bed to £1,571 psf for a 2 bed. It is interesting to note that all of the units assessed are located above the 15th floor.

6.44. It should be noted that this site is considered to be in a slightly inferior location to the Scheme, as it is not so centrally based and does the have the benefit of a large area of public open space. The potential (and achieved values) can therefore be considered to be on the conservative side in comparison to what may be possible on the scheme.

6.45. Whilst there is an element of the information being treated with caution when assessing the potential values, we do consider that the evidence provided, with marginal adjustments, can be useful in the round.

Affordable Housing

6.46. In relation to the affordable housing values we have reviewed the tenure mix proposed and comment on pricing.

6.47. [redacted]

6.48. [redacted]

[redacted]

6.49. [redacted]

Preliminary Conclusions

6.50. [redacted]

6.51. [redacted]

6.52. In addition, given the infrastructure assumptions, public realm and place making benefits of the Scheme, we are of the view that a regenerative impact will be achieved overall. This will only seek to increase the sales values.

6.53.

The analysis and breakdown of residential pricing provided by the JV Applicant is limited. A Sales Agents Report, in our view would have robustly dealt with the schemes pricing. In the absence of this, we therefore consider residential values should be adjusted

6.54. We appreciate that there are over 1,364 units to value but greater detail of pricing could have been undertaken and presented. It is unclear as to the reasoning why this exercise was not undertaken given importance of the residential value on the viability of the Scheme.

6.55. We accept that any uplift in value on each unit will vary, relative to its location within the Scheme. We have however tested a holistic upside through the sensitivity testing in section 11.

6.56. The commentary provided by BNPP on market movements in these boroughs since 2012, supports our view that the sales values have been underestimated. In the absence of any comprehensive analysis of pricing, there is no definitive market evidence to suggest that upwards adjustments should not be made [redacted]

6.57. [redacted]

7. Costs and Construction Programme

Introduction

7.1 In this section we review the cost inputs within DS2's FVA 2 (including the updated cost as of February 2016) and BNPP due diligence exercise. We provide a summary overview of the inputs, then review the source of each element, and finally provide comment and analysis of each. We also comment on the assumed development timeframe.

Summary of Information Provided

Construction costs

7.2 As part of FVA 2 a full 'Budget Estimate' cost report, dated 22 June 2015, was provided. This was prepared by G&T. These costs were separated out into build costs and standard costs for construction of the development.

7.3 After the application was called in we made a series of requests to both DS2 and the JV Applicant to provide further justification in relation to a number of cost inputs, in particular where BNPP raised concerns in its due diligence report over the reasonableness of the cost. During the course of February 2016 the JV Applicant through DS2 and G&T provided us with further justification and advised on the update to the costs that had occurred since June 2015, when the cost report was originally prepared, taking into consideration market movements.

7.4 The build costs included base costs, abnormals, public realm and park, preliminaries and overheads and profits. The aggregated costs are set out below.

Table 16: Construction cost assumptions summary

[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]		[redacted]	[redacted]
[redacted]		[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]	[redacted]

Source: DS2 FVA2 and G&T Cost Report (June 2015)

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7.5 A further summary of the items included in the abnormal costs is provided in the following table:

[redacted]

[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
[redacted]	[redacted]	

[redacted]

Construction and Developer Contingency

7.6 [redacted]

7.7 The boroughs initially instructed Synergy LLP cost consultants to review G&T's Budget Estimate. BNPP stated in their review that Synergy LLP considered that the base costs should be reduced. We were not provided with the report prepared by Synergy LLP.

7.8 We note that WTP were instructed by the boroughs to review G&T's Budget Estimate of June 2015. BNPP have regard to WTP's comments in Due Diligence 2.

7.9 [redacted]

[redacted]

[redacted]

[redacted]

Construction Programme

7.10 A detailed construction programme was provided in FVA2. This was not amended to reflect the revised programme agreed as part of the final offer. The following table is a summary of DS2s construction programme, which has been adapted to reflect the final offer.

Table 18: DS2's assumed development programme

Phase: Block	Date	Duration	End
Phase 1:			
Block C	Jul-16	48	Jul-20
Block E			
Block H	Apr-17		Jan-20
Phase 2:			
Block A	Jul-20	36	Apr-23
Block B	Oct-20		Jul-23
Phase 3:			
Block F	Apr-22		Oct-24
Block G	Jul-21	42	Apr-24
Block L	Jul-21		Oct-22
Phase 4:			
Block I	Oct-24		Jul-26
Block J	Oct-24	63	Jul-26
Block D	Jul-26		Jan-30
Phase 5:			
Block K	Jan-30	30	Jul-32

Source: DS2

7.11 The construction timeframe provided assumes the c.1,364 residential units will be constructed and sold in a period of 17 years.

Planning and CIL obligations

7.12 The table below is the final position in relation to financial planning obligations and CIL.

[redacted]

[redacted]

Source: JV Applicant Final Offer

7.13 The following table provides further detail on the breakdown of the S106 financial obligations.

Table 20: Detailed Section 106 Financial Obligations

Section 106 Contributions Breakdown	S106 (LBTH)	S106 (LBH)	S106 (TfL)
Shoreditch Triangle			£5,900,000
Bethnal Green Road Pedestrian	£250,000		
Travel Plan monitoring*		£12,000	
Carbon offset payment (site	£837,000	£837,000	
Monitoring fee **	£10,000	£10,000	[£1,500 per Tfl approval]
Cycle docking stations			£600,000
Employment, skills and training ***	£1,162,497	£2,813,041	
[Cycle Improvements]****	£550,000		
*Assuming 3 phases in LBH **Currently unknown number of Tfl Approvals ***Subject to justification by LBTH and LBH ****Subject to justification by LBTH	**£2,809,497**	**£3,672,041**	**£6,500,000**

7.14 There is also a requirement to provide a number of planning obligations that are not in the form of a cash receipt, which are summarised as follows:

i Affordable Workspace: 10% of (the NIA office floor3 space) within plots A, B and K with a 20% discount from market rents;

[3] We have made the assumption that this constitutes 10%of GIA of Office floor space

ii Doctors Surgery: 1,000 sq ft at a market rent on a 25 year term; and

iii Ideas Store: 4,165 sq ft at a peppercorn rent for 30 years;

iv Apprentices Provision: 150 apprentices employed across the site during the construction period, for a period of not less than 13 weeks. The Applicant will be required to submit various monitoring reports at different stages of the process and expected to pay the councils Apprentices Payments of £7,000 per person, in respect of the shortfall in Apprentices provided

Analysis and comment

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

7.17 G&T made a series of requests for further clarifications from WTP, which we understand were never resolved. We do not consider these to be matters to be of a sufficient magnitude to significantly impact the viability of the Scheme.

7.18 We requested an update to the construction costs to reflect the position as at February 2016. The update was in the form of indexation, which is a commonly used and appropriate practice in adjusting costs over time. A summary of the update to the 'Budget Estimate' June 2015 is shown in the table below.

7.19 [redacted]

[redacted]

[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]
[redacted]	[redacted]

Source: G&T February 2016

7.20 On discussion with BNPP and our own analysis of the construction and development programme, we requested that DS2 provide further justification for the construction period of each block. We summarise this as below:

i **Phase 1 Plot C**

a 38 storey scheme built off a podium over the East London Line, adjacent to the listed arches to the south and a historic boundary wall to the north. Significant site constraints will affect the construction programme including the availability of loading and storage areas.

ii **Phase 1 Plot E**

a Access to the site is restricted due to it being land locked to the north and south and Brick Lane being located to the east. The only access is from Sclater Street. The building sites in close proximity to and partially underneath the East London Line which will have heavy restrictions on the development of the site by Network Rail.

iii **Phase 1 Plot H**

a The construction of the one acre park will be restricted by the preservation of listed buildings including the Braithwaite Viaduct and the arches which surround this element of the site. The plot also runs alongside the railway cutting and above the Surburban Line Tunnel, which will add further complications from working with Network Rail and potentially requires engineering hours.

iv **Phase 2 Plots A and B**

a East London Line running the length of both plots on the eastern side means limited space for unloading and laydown area. An assumption has been made that the junction between Plot A and B will be used as the logistics area, but this is limited and can only be serviced by 'just in time' deliveries, which could have an impact on the progress of the works.

v **Phase 3 Plots F, G and L**

a The site is constrained by the location of Commercial Street to the west, the construction of plots A and B to the north and Braithwaite Street to the East. It abuts the rail cutting and tunnels to the south which services six railway lines into Liverpool Street Station and a further tunnel for the Central Line which cuts through the site;

b Plot G will be constructed first and is expected to complete within 33 months;

c Plot F follows in sequence commencing after completion of the podium structure within 42 months;

d Plot L will be constructed at the junction of Commercial Street and Shoreditch High Street and includes the restoration of the listed Oriel Gateway and remaining gate structure.

vi **Phase 4 Plots D, I and J**

a All plots are severely constrained due to location and close proximity to those sites that will already have been completed – Plot C to the west, Plot E to the East and Sclater Street to the north;

b Plots I and J commence in conjunction with D;

c Plots I and J also run alongside the open cut railway and above the Suburban Line Tunnel, which will add further complications from working with Network Rail and potentially require engineering hours.

vii **Phase 5 Plot K**

a Plot K was an additional plot that was added to the original scheme and presented in the amended scheme of July 2015 in FVA 2;

b It is a significant building that will be built above the open cut railway including four live rail lines;

c The area along Quaker Street and South of the Suburban Line tunnels will need to be piled. This will require liaison with Network Rail to enable access.

7.21 We have adopted the CIL figures provided and calculated by DS2, and the JV Applicant in FVA 2. As the detail of the Scheme evolves then these may be subject to change, but will only have a material impact on viability should the Scheme change significantly.

Preliminary Conclusions

7.22 We note the different views raised by the respective cost consultants on costs and whilst there may be variations in the Scheme, we do not consider these variations warrant another full cost review. The necessary cost parameters have been recognised and there is broad agreement between DS2 and BNPP on the quantum of the majority of them. We therefore consider it reasonable to accept G&T's Budget Estimate of June 2015, indexed to February 2016, as reasonable costs.

7.23 Our role in reviewing the viability of the Scheme is not to assess the reasonableness of the particular costs, but to review the overall level of the financial contribution alongside the affordable housing offer. We are not instructed to identify what costs should be apportioned to S106 items; rather we comment and conclude as to whether the overall "pot" which has been offered by the JV Applicant and the level of contribution is the maximum reasonable that the Scheme can afford.

7.24 We are not seeking to alter the abnormal or additional development costs and agree with the views of both consultants on the quantum of the cost.

7.25 The concern BNPP raise is the treatment of the cost having regard to the Site Value, and whether it is right that the abnormal or sunken costs are reflected in the Site Value. It is our view that the Site Value reflects the value of the Site[4], and disregards the costs associated with the East London Line Extension Works and Suburban Line Tunnel Upgrade. This is discussed further in Section 8.

7.26 [redacted]

7.27 [redacted]

7.28 [redacted]

7.29 Whilst there is likely to be a degree of variance in the programme, our role is to make

[4] Having regard to NPPF. PPG and RICS Site Value definition in GN 94/12

sure the assumptions put forward by DS2 are reasonable, and not to comment on the range of possible scenarios which could take place.

7.30 Clearly, any alteration in the distribution of the S106 payments will alter the financial makeup and therefore the viability of the Scheme. Given that there have been a number of S106 meetings between the JV Applicant and the GLA during the call-in to discuss the detail of the S106 Agreement, the timings of the payment and delivery of the obligations have been agreed, which have been modelled.

8. Site Value

Introduction

8.1. This section sets out the underlying basis of the adopted Site Value. Our views are formed having regard to the NPPF, PPG, GLA Housing SPG and RICS GN 94/12.

8.2. We review DS2's opinion and justification of Site Value in its FVA, and we also provide comment where necessary on the views of BNPP.

8.3. We have, in addition, provided further analysis and assessment of other evidence we are aware of, to help inform our views.

Overall approach

8.4. In arriving at a Site Value we have had regard to the following:

- National planning policy and guidance and RICS best practice, including;
- Comparable transactions; and
- All other matters which the market would have regard to in arriving at a Market Value (including existing, alternative uses and site constraints).

Planning Practice Guidance

8.5. The PPG states:-

"Central to the consideration of viability is the assessment of land or site value. Land or site value will be an important input into the assessment. The most appropriate way to assess land or site value will vary from case to case but there are common principles which should be reflected. In all cases, <u>land or site value should</u>:

- *reflect policy requirements and planning obligations and, where applicable, any Community Infrastructure Levy charge;*

- *provide a competitive return to willing developers and land owners; and*
- *be informed by comparable, market-based evidence wherever possible. Where transacted bids are significantly above the market norm, they should not be used as part of this exercise"*

8.6. The PPG describes the meaning of a "competitive return to a willing land owner" as follows:

"A competitive return for the land owner is the price at which a reasonable land owner would be willing to sell their land for the development. The price will need to provide an incentive for the land owner to sell in comparison with the other options available. Those options may include the current use value of the land or its value for a realistic alternative use that complies with planning policy."

RICS Guidance Note 94/12

8.7. Site Value is defined in GN 94/12 as follows (para 2.8):-

"Site Value should equate to the Market Value subject to the following assumption; that the value has regard to the development plan policies and all other material considerations and disregards that which is contrary to the development plan".

8.8. The GN 94/12 highlights that Site Value must, by definition, be at a level where the landowner is willing to sell at a competitive return as recognised by the NPPF. It also states that Site Value "has regard" to policy. Site Value therefore by definition is not unrestricted when compared to Market Value as defined the RICS Red Book. The degree of variance will be subject to a judgement, having regard to the circumstances in each instance.

8.9. In terms of infrastructure and enabling costs, we note that the RICS GN states the following (para. 3.6.2):

"Where there has been historic expenditure on a development site prior to receiving planning permission, these can be included in a development appraisal. This is highly relevant with certain regeneration site, where cost is not reflected in Site Value. Care,

however, must be taken in arriving at a Site Value that the effect of this expenditure should be ignored. In many instances the practitioner will note the expenditure as being reflected in the Site Value arrived at and therefore the historic cost (for example remediation works) will not appear explicitly in the appraisal. Clearly, the objective is that there should be no double counting".

8.10. We understand from the FVA 1 and 2 that the vendor of the Site has incurred enabling costs for the development as presented in section 7.

DS2

8.11. On request, a summary of the purchase agreement was provided by the JV Applicant. This broadly represented the acquisition price (with interest). Further details of the purchase agreement are not disclosed in this report due to confidentiality. We confirm that we have had regard to this information in our review and assessment of Site Value.

8.12. DS2 have adopted a Site Value of £83m based on an analysis of comparable land transactions. DS2 analysed the following transactions:

- Aldgate Place
- One Commercial Street
- 61-75 Alie Street (Altitude Aldgate)
- Huntington Industrial Estate, Bethnal Green Road
- Goodmans Fields, Leman Street
- 21 Wapping Lane
- Silk Gardens, Partimer Street
- Avante Garde, Bethnal Green Road

8.13. The transactions are all within the postcodes of E1 or E2. The transaction dates range from 2007 to 2014 and the purchase prices have not been indexed to reflect an assumed up-to-date market position.

8.14. DS2 provided the most detailed information on the Aldgate Place transaction.

8.15. DS2 have not provided an EUV or Alternative Use Valuation ("AUV") of the Site.

BNPP

8.16. BNPP adopted a Site Value of £20 million based on an EUV of the site.

8.17. Due Diligence 2 refers to the London Draft Interim Housing SPG and the conclusion that: *"on balance the GLA has found that the 'Existing Use Value plus' based approach is generally more helpful for planning purposes and supports this approach" (para 4.4.28).*

8.18. BNPP use LBTH's 'Site and Place Making Development Plan Document – Site Viability Testing' which was published in February 2011 as the foundation of their opinion of Site Value. The area wide planning document, only for LBTH, concludes that in 2011 the site value was £17.8 million, based on industrial/ storage use. BNPP were commissioned to prepare this area wide report for LBTH.

8.19. BNPP have allowed for inflation between 2011 and 2016, increasing the Site Value to £20m. It is not clear whether BNPP include the Site's land in LBH in its valuation of £20m. On review of BNPP's appraisal, we can only assume that its Site Value assumption encompasses the entire Site, across both boroughs.

8.20. BNPP consider the comparative approach adopted by DS2 to:

"Demonstrate a significant lack of transparency in terms of how process paid for sites have been arrived at significant differences in site characteristics" (par. 5.1).

8.21. BNPP consider that adopting a Site Value based upon land transactions that assume forecast values and costs will result in an inconsistent comparison.

Analysis and Comment

8.22. DS2 completed a high level analysis of various land transactions, on the following basis:

- £Land Value / Acre
- £Land Value / GEA

8.23. There is a considerable degree of variance in comparability associated with DS2's referenced comparable transactions, albeit they are all within the same local postcode. Whilst the locational characteristics are extremely important in analysing land transactions against the Site's value, it is reasonable to compare sites which are wider afield where local site comparability is poor in relation to of size of site; density/scale/massing; a purchase with or without planning permission; and, the historical market conditions, amongst other factors. So far as DS2's justification is concerned, we consider the most relevant to be:

- Aldgate Place; and
- One Commercial Street.

8.24. The transactions have been analysed on the following basis:

- All purchase prices have been indexed in line with the Savills Land Index;
- £ per acre;
- £ per sq ft on the proposed NIA;
- £ per sq ft residential and commercial NIA;
- £ per total residential units and £ per private unit.

<u>Aldgate Place</u>

8.25. The site extends to 0.79 hectares (1.95 acre) and is located approximately 0.8 miles from the Site. The site was purchased by a joint venture between [redacted] for [redacted] in July 2014. Planning permission was achieved in July 2013 for the development of:

- Demolition of existing buildings and creation of a mixed use development comprising of three towers of 22, 25 and 26 storeys and a series of lower buildings ranging from 6 to 9 storeys;
- Provision of 463 residential dwellings including 35% affordable housing;
- Office Use (B1);
- Hotel Use (C1);
- Retail Use (A1-A4);
- Leisure (D2);
- Public realm and new streetscapes

8.26. This transaction is considered useful due to its location and mix of uses, including the provision of a number of towers (one up to 26 storeys). The affordable housing provision is 35%. The site was purchased with the benefit of planning permission.

8.27. The indexed purchase price of [redacted] equates to [redacted] per acre and [redacted] on the assumed proposed residential NIA. On a residential unit bases, the price equates to [redacted] per unit or [redacted] per private unit.

<u>One Commercial Street</u>

8.28. The site extends to 0.111 hectares (0.27 acre) and is located approximately 0.6 miles away. The site was purchased by Redrow Homes Limited for £38,950,000 in January 2012. Planning permission was achieved in March 2005 for:

- Demolition of existing buildings and creation of a mixed use development comprising of three towers of 22, 25 and 26 storeys and a series of lower buildings ranging from 6 to 9 storeys;
- Provision of 217 residential dwellings including 33% affordable housing;
- 23 storey building (with roof terrace);
- 1,367 m2 of Retail (A1-A3) or Leisure D2 at ground floor;
- 1,609 m2 of either class (A1-A3, B1, D1) or 8,430 m2 of Offices (B1) on the 2nd to 6th floors;
- New entrance to Aldgate Underground Station.

8.29. Location and mixed use nature, including the provision of towers (one up to 23 storeys) across the affordable housing provision of 33%, all provide comparability.

8.30. The indexed purchase price of £55,960,862 equates to £207,262,450.11 per acre. It also equates to £129.49 per sq ft on the assumed proposed NIA. On a residential unit bases, the price equates to £257,884.14 per unit or £385,936.98 per private unit.

8.31. We have plotted the above transactions on the graphs below which compares the price paid expressed in terms of £ per acre, £per sq ft on the proposed residential NIA, £ per residential units and £ per private units. The averages have been calculated omitting DS2's Site Value assumption for the Site.

Figure 1: Land Transactions compared against Site - £/ Acre

GRAPHIC REDACTED

8.32. The average value on an indexed price per acre basis equates to [redacted] per acre, against DS2's £8m per acre. Because of the variations in areas and densities for these comparables, assessment on a £/ac basis in this area is a crude measure, helpful only as a 'sense' check.

8.33. In addition to assessing the comparable development sites on a £ per acre basis, we have also analysed the comparable sites on a Proposed Residential NIA £ per sq ft basis. This is a more appropriate way of measuring comparable market sales evidence in this type of development. This is shown in the figure below.

Figure 2: [redacted]

GRAPHIC REDACTED

8.34. We understand the JV Applicant is proposing approximately [redacted] of residential space at the Site and therefore the assumed purchase price of [redacted] equates to [redacted] residential NIA. The indexed average value of 'Proposed Residential NIA £ per sq ft' of the comparable transactions equates to [redacted]

8.35. There is a range of between [redacted]

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Figure 3: Land transactions compared against Site - £/Unit

GRAPHIC REDACTED

8.36. The Scheme is to comprise of 1,356 units of which 1,215 are proposed as private. The assumed Site Value therefore equates to [redacted] per private unit.

8.37. Based on the comparable evidence the average price per unit is [redacted] On a residential unit basis the Site Value could be in a range of between [redacted], based on the lower range [redacted] per unit and [redacted], based on the higher range of [redacted] .The mid-point Site Value is [redacted]

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Figure 4: Land transactions against Site - £/Private Unit

GRAPHIC REDACTED

8.38. The Scheme is to comprise of 1,215 are proposed as private. The assumed Site Value therefore equates to [redacted] per unit or [redacted] per private unit.

8.39. The average price per unit is [redacted]. The lower range of £[redacted] per unit and [redacted] based on the higher range of [redacted]

8.40. We have also had regard to the following transactions, not referenced by DS2:

- M&S Depot, White City;
- BBC Television Centre (development land), W12;
- Battersea Gasholders, Nine Elms;
- London Dock (News International), Wapping; and
- Surrey Quays Leisure Site.

8.41. These transactions have been selected in line with the following criteria:

- Location;
- Size;
- Purchased without planning permission since 2011;
- Affordable housing provision onsite;
- Sales values in excess of £1,000 psf;
- Site which requires significant enabling works in order for the development to progress;
- Significant proposed development, including number of residential units;
- Existence of a tower of similar height.

<u>M&S Depot, White City</u>

8.42. St James Group acquired the Site from Marks and Spencer plc for an agreed sum of £100 million, with a leaseback to Marks and Spencer plc / Busyexport Ltd (a subsidiary of Marks and Spencer plc) for a term of five years with a mutual break in year three. The purchase was completed in July 2013.

8.43. The Site was purchased unconditionally but with a series of deferred payments. The present value of the future payments is calculated to be £88.6 million. In order to account for inflation in development land prices since the transaction, we have indexed the adjusted purchase price for the site up to Q4 2015 using the Savills Development Land Index. This results in an indexed purchase price of approximately £109 million.

8.44. The indexed purchase price of £109 million equates to £10.5 million per acre or £96 per sq ft on the proposed residential net internal area (NIA) of 1,135,222 sq ft. On a proposed residential unit basis, the indexed purchase price equates to £74,595 per unit or £84,062 per private unit.

<u>BBC Television Centre (development land), W12</u>

8.45. The existing property comprises the iconic television studios complex previously occupied by the BBC, located in the London Borough of Hammersmith and Fulham. The entire site measures approximately 14 acres. The site is situated immediately south west of the M&S Depot site, on the opposite side of Wood Lane, also forming part of the White City Opportunity Area. The site was purchased [redacted] without planning permission for redevelopment.

8.46. We understand that the transaction comprised [redacted], with a [redacted]. A [redacted]

8.47. As part of the transaction [redacted] was agreed relating to the [redacted]. In order to analyse the transaction we have therefore [redacted].

8.48. We understand that a value of [redacted] was attributed to [redacted]. [redacted]

[redacted]

8.49. Indexing this comparable in line with the other evidence gives an indexed purchase price for the BBC development land [redacted]

8.50. The indexed purchase price of [redacted]. On a square foot basis this equates to [redacted] on the proposed residential NIA. It equates to [redacted] per proposed residential unit, or [redacted] per private unit. The proposed development density equates to 76 units per acre.

Battersea Gasholders, Nine Elms

8.51. The Battersea Gasholders site comprised a former natural gas facility operated by the National Grid extending to 4.99 acres. The site was decommissioned in 2012 and is currently being redeveloped. The Site is located on Prince of Wales Drive on the eastern edge of Battersea Par, to the south of Battersea Power Station, in the London Borough of Wandsworth.

8.52. The site was purchased without the benefit of planning permission in September 2013. The purchase price was confidential but was reported to be [redacted]. Planning permission was subsequently granted for a residential-led mixed-use scheme

8.53. In order to account for inflation in development land prices since the transaction, we have indexed the adjusted purchase price for the site up to Q4 2015 using the Savills Development Land Index. This results in an indexed purchase price of approximately [redacted]

8.54. The indexed purchase price of [redacted] equates to £[redacted] per acre. On a sq ft basis, this equates to [redacted] on the proposed residential NIA. On a residential unit basis, the price equates to [redacted] per unit or [redacted] per private unit. The proposed development density equates to 168 units per acre.

London Dock (News International), Wapping

8.55. The existing property was previously home to News International. The site is located in

LBTH. The site extends to 15.07 acres (6.1 hectares). It was purchased by St George Central London Ltd without the benefit of planning permission for £143.9 million in May 2012. Outline planning permission has since been granted for a maximum of 2,568,014 sq ft (GEA) of development.

8.56. We have been unable to source the floor area of the residential space on an NIA basis and have assumed a gross to net ratio of 80% for the purpose of our analysis. The indexed purchase price of £201 million equates to £13.5 million per acre. On a sq ft basis, this equates to £133 on the proposed residential NIA. On a residential unit basis, the price equates to £111,714 per unit or £128,818 per private unit. The proposed development density equates to 119 units per acre.

Surrey Quays Leisure Site

8.57. The site, which extends to 8.50 acres (3.44 hectares), currently accommodates two large leisure buildings comprising an Odeon multi-screen cinema, a bingo hall and a bowling alley; three small restaurants; and an unoccupied derelict public house. The property is located in Canada Water on the Rotherhithe Peninsular approximately 1 km to the east of the subject property in the London Borough of Southwark. The site was purchased by British Land with the benefit of planning permission in March 2015 for £135 million.

8.58. The purchase price of £135 million equates to £300 per sq ft on the assumed proposed residential NIA. On a residential unit basis, the price equates to £265,226 per unit or £353,403 per private unit.

8.59. The following table provides a summary of these comparable land transactions.

Table 22: Summary of Comparable Land Transactions

Site	Date	Indexed Price	Price £/unit	Price £/sq ft NIA	Price £/sq ft Resi NIA	£/Private Unit
M&S White City	Jul-13	£109,280,972	£74,595	£91	£96	£84,062
London Dock (News International)	May-12	£201,085,638	£111,714	£107	£133	£128,818
Battersea Gasholders	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]
BBC Television Centre	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]	[redacted]

Source: Gerald Eve Research

8.60. We have excluded from our analysis British Land's purchase of the Surrey Quays Leisure Site. When plotted against the evidence shown above, this transaction represents a clear anomaly which skews the data upwards to what we consider an unreasonable level. The reason for this is likely to be British Land's wider aspirations for this location having already acquired Surrey Quays Shopping Centre and Harmsworth Quays. By assembling these sites, covering approximately 50 acres, British Land hope to create one of the largest mixed use regeneration projects in London. As such, the Surrey Quays Leisure Site transaction would appear to constitute a special purchase which would likely explain the reason for this being a clear outlier when compared to the evidence above.

8.61. We have plotted the above transactions on the graphs below which compares the price paid expressed in terms of £ per acre, £per sq ft on the proposed residential NIA, £ per residential units and £ per private units. The averages have been calculated omitting DS2's Site Value assumption for the Site.

Figure 5: Land transactions compared against Site - £/ Acre

GRAPHIC REDACTED

8.62. The average value on an indexed price per acre basis equates to [redacted] per acre. This is higher than that of the Scheme where the purchase price equates to approximately [redacted] per acre. Applying this average to the area of the Site (10.3 acres) results in a site value of £[redacted]

8.63. In addition to assessing the comparable development sites on a £ per acre basis, we have also analysed the comparable sites on a Proposed Residential NIA £ per sq ft basis. This is shown in the below graph.

Figure 6: [redacted]

GRAPHIC REDACTED

8.64. We understand that the JV Applicant is proposing approximately 1[redacted] of residential space at the Site and therefore the assumed purchase price [redacted] equates to [redacted] per sq ft residential NIA.

8.65. The indexed average value of 'Proposed Residential NIA £ per sq ft' of the comparable transactions equates to [redacted]

8.66. On a residential NIA basis the Site Value could be in a range of between [redacted], based on the lower range of [redacted] and [redacted], based on the higher range of [redacted] .The mid-point Site Value is £[redacted].

8.67. The following graph demonstrates the comparable land transactions, analysed on a total residential unit basis.

Figure 7: Land Transactions against Site - £/ Unit

GRAPHIC REDACTED

8.68. The Scheme is to comprise of 1,356 units of which 1,215 are proposed as private. The assumed Site Value therefore equates to [redacted] per unit or [redacted] per private unit.

8.69. Based on the comparable evidence the average price per unit is [redacted]. On a residential unit basis the Site Value could be in a range of between [redacted], based on the lower range of [redacted] per unit and [redacted], based on the higher range of [redacted] .The mid-point Site Value is [redacted].

Figure 8: Land Transactions against Site - £/ Private Unit

GRAPHIC REDACTED

8.70. Adopting the average £ per private unit figure of [redacted] the above evidence suggests that the Site Value could equate to approximately [redacted]

8.71. The evidence varies chronologically i.e. the averages have been calculated using transactions over a period of time, within which there will undoubtedly have been improvements in the market.

Further Analysis

8.72. We have also considered the purchase price as a percentage of GDV as a knowledgeable landowner would be aware of the likely sales values and would expect a land price to have some correlation with house price movements.

8.73. The graph below illustrates a benchmarking exercise we have undertaken on a number of strategic sites across London (N.B. these are not the comparables set out earlier in the Section). It sets out the actual Site Values adopted for financial viability purposes against the total GDV of the planning schemes. The sites are anonymous for reasons of confidentiality.

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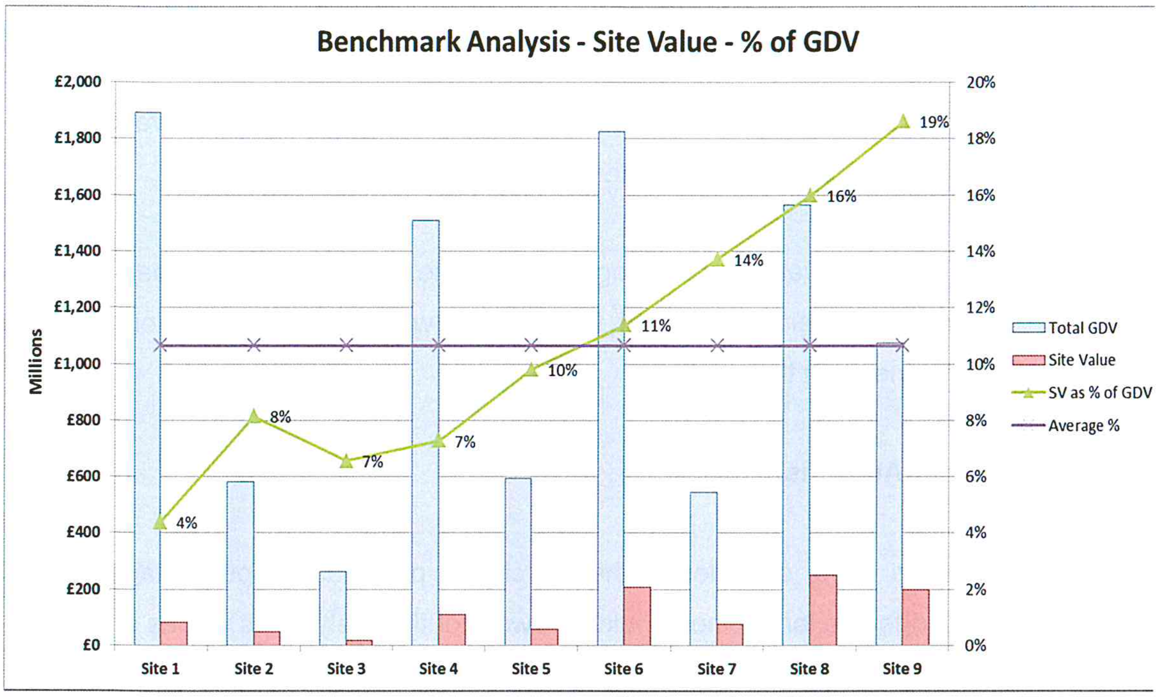
Figure 9: Site Values as a percentage of total GDV



8.74. The above figure illustrates the relationship between Site Value and total GDV. It shows that from the sample selected this ranges from 4% to 19% with the average being 11%.

8.75. We understand that in the instance of the Site, the total GDV is likely to be in the region of c. £1.8 billion, therefore the net Site Value of £83 million reflects 4% of GDV, which is illustrated at Site 1.

8.76. When we consider Site Value of £150 million, it can be concluded that the Site Value represents 8% of GDV, which remains below the average of 11%.

Preliminary Conclusions

8.77. In arriving at our opinion of Site Value, we have taken into account the NPPF, PPG and GN 94/12. We have looked at comparable market evidence and considered this in a number of ways in the context of the proposed Site Value put forward by DS2 on behalf of the JV Applicant, and the opinions of BNPP.

8.78. In applying the PPG, noting that the willing seller requires a competitive return and providing an evidence base of comparable evidence, we consider that DS2 are consistent with the practice guidance and GN 94/12 definition of Site Value. In relying upon comparable market based evidence we are of the view that if the Site was placed on the market tomorrow, bids would be received at levels in excess of DS2's opinion of Site Value. In our view, £83m reflects a level that would be towards the lower end of a possible range of bids. We disagree with BNPP's views that DS2 have not reflected the impacts that the significant (and acknowledged) enabling costs will have upon Site Value. Given the market based analysis, we are satisfied that the £83m fully reflects the absence of enabling and development costs. A Site Value that did reflect these costs would be significantly in excess of £83m.

8.79. We are of the opinion that DS2's Site Value has been determined in accordance with the requirements of the PPG. In this instance we fundamentally disagree with BNPP's views that £20m would meet the definition of a competitive return to a landowner. We have not identified sufficient justification or reasoned views in BNPP's reports to the contrary. Reliance on an area-wide study prepared by BNPP with no real valuation principles justifying the level of existing use, is, for the purpose of the Review, wholly inadequate and should not be relied upon. Whilst in some development circumstances assessment by reference to EUV may be appropriate, it should in all cases be sense checked against other valuation approaches. This is recommended in PPG as well as the RICS GN on Valuation of Development Land (VIP12). A narrow, singular approach unsupported by any evidence is inappropriate. BNPP's assessment of benchmark does not comply with NPPF- the value is clearly well below a 'competitive return' that a landowner would reasonably expect.

Table 23: Site Value Analysis

Price £/unit	Price £/private unit	[redacted]	Avg Price £/acre
£157,008,542	£158,349,831	[redacted]	£140,987,650

Source: Gerald Eve Analysis

8.80. The analysis of the comparable transactions illustrates that the Site Value could potentially lie between a range of £140 million and £159 million.

8.81. DS2 also point to the relationship between Site Value as a percentage of gross development value, which in this case, is relatively small, and which is illustrated in **Figure 9**.

8.82. GE have taken in to account the information and approaches by DS2 and BNPP in arriving at a balanced assessment of site value. GE considers that the assessment by DS2 does not overstate the site value, and can therefore be accepted.

9. Review of Financial Appraisal

9.1. We have reviewed the methodology, value, construction costs and Site Value in the previous sections. Below we set out and review the Scheme appraisal. In the next section we consider the sensitivity of this and the impact upon the proposed final offer (Affordable Housing and Section 106 obligations).

Summary of Information Provided

9.2. DS2 has used Argus Development software to undertake its financial assessment, which is an accepted appraisal tool. BNPP has also used Argus Development software, and its appraisal provides amended inputs where there are areas of disagreement, or inaccuracy.

Analysis and Comment

9.3. Through the process of reviewing the documentation and an understanding of the respective positions of both viability consultants we are of the view that the majority of the inputs put forward by DS2 are reasonable. We have commented throughout this report about the possible variance in inputs and possible upper and lower levels. We are therefore of the view, having regard to our comments above, that the following adjustments should be made:

[redacted]

[redacted]

[redacted]

9.4. As a result of these adjustments, and having regard to the JV Applicant's Final Offer, the summary of the present day appraisal is shown in the table below.

Table 24: Gerald Eve Appraisal Outputs – Present Day

	GE **Present Day**
IRR	[redacted]
Affordable housing contribution	**The Final Offer**
S106 obligations	**The Final Offer**

Preliminary Conclusions

9.5. With regard to GDV and costs, we comment on these in the previous sections of the Review, together with our methodology and approach.

9.6. [redacted]

9.7. [redacted]

9.8. [redacted]

9.9. It is stressed that the summary in Table 24 is on a present day basis. However, we consider that a growth basis is more appropriate in analysing the viability of the Scheme, in line with PPG:

"...where a scheme requires phased delivery over the medium and longer term, changes in the value of development and changes in costs of delivery may be considered. Forecasts, based on relevant market data, should be agreed between the applicant and local planning authority wherever possible."

9.10. In the next section we make adjustments to our appraisal considering the outturn approach to assess the ability of the Scheme to meet the planning obligations.

10. Growth and inflation

10.1 In view of the magnitude of the Scheme and the timeframe over which it is to be delivered, we consider it necessary to reflect anticipated future movements in both costs and values in order to understand the outturn approach to viability. This can then be compared with a present-day approach.

10.2 This section provides our underlying assumptions associated with the forecasting of cost and value inflation over the course of the proposed development.

Cost inflation

10.3 Rates used in the compilation of cost estimates are of the date it was undertaken and therefore do not take account of the impact of any inflation that may occur during the procurement or construction periods. The procurement and delivery of the works is set against a back drop of anticipated rising prices. Due to the long duration of the works and phased delivery the inflation on costs will be real and it is correct to build them into an appraisal.

10.4 Cost consultants can undertake analysis which identifies elemental costs spread over the proposed construction programme to deduce an anticipated inflationary exposure linked to the delivery programme. Whilst none has been prepared here we have experience in using this approach in other major regeneration projects.

10.5 We can apply an additional inflation factor throughout the construction phase to reflect building cost inflation incurred by the contractor in the course of his business, the principal ones being those for labour and materials. The combination of tender price inflation up to start on site and building cost inflation throughout the construction phase most accurately reflects the true grown construction cost for the scheme in the growth/outturn appraisal.

10.6 We have assumed building cost inflation throughout the construction phase to broadly in line with BCIS forecasts.

Table 25: Adapted from BCIS TPI construction forecasts

TPI Assumption	Year
3.3%	2016
4.6%	2017
5.1%	2018
5.1%	2019
5.2%	2020
4.0%	2021+

Residential Sales Growth

10.7 We have incorporated growth into the private residential units of the Scheme in our appraisals, in order to assess the impact of changing capital values on the Scheme's viability.

10.8 In determining appropriate growth rates to apply to residential values, we rely upon data provided by the major property consultancy houses and our own in house research.

10.9 Each residential agency / research team has its own approach to analysing the London residential market and submarkets. Most London residential research typically differentiates between the property locational and product characteristics.

10.10 The residential sales value growth rates assumed throughout the scheme are set out in the following table:

Table 26: Residential Sale Growth Rates –

Residential Sale Growth Rate	Year
5.0%	2016
3.8%	2017
4.3%	2018
4.5%	2019
5.0%	2020
4.5%	2021+

Source: GE

10.11 This is an assumption of overall market growth and does not take account of any regeneration effect that is likely to arise throughout the delivery of the scheme.

10.12 We have assumed that a developer will dispose of the affordable element to a RP on practical completion of each relevant block. We have therefore assessed potential growth in disposal receipts (capital values) between 2016 and 2020.

10.13 RPs are obliged to reduce rents by 1% per annum over this period in accordance with the Housing and Planning Act 2016.

10.14 The levels of growth that have been assumed for the on-site affordable housing are set out in the following table:

Table 27: Affordable Housing Growth Rates

Affordable Housing Growth Rate	Year
0%	2016
0%	2017
0%	2018
2%	2019
2%	2020

Source: GE

Commercial Growth Assumptions

10.15 The retail sales value growth rates assumed throughout the scheme are set out in the following table:

Table 28: Commercial Growth Assumptions

Year	Retail Growth Rate	Offices Growth Rate
2016	0.0%	6.4%
2017	2.0%	3.3%
2018	5.0%	3.2%
2019	6.5%	3.0%
2020	6.5%	3.0
2021	4.0%	4.0%

Source: GE

10.16 The financial appraisals of the scheme can be compared and summarised as follows:-

Table 29: Gerald Eve Appraisal Outputs - Growth

	[redacted]	[redacted]
[redacted]	[redacted]	[redacted]
Affordable housing contribution	**Final Offer**	**Final Offer**
S106 obligations	**Final Offer**	**Final Offer**

10.17 The above is measured against the risk profile set out in paragraph 4.26. It also is in accordance with the need to update financial information, as discussed in paragraph 1.5.

10.18 In the next section we make adjustments to our appraisal considering the sensitivity around the output in order to consider the ability of the Scheme to meet the planning obligation

11. Sensitivity Analysis

11.1 There are various methods and approaches that can be employed to measure an appraisal, from basic two-way sensitivity analysis to more sophisticated simulation analysis. In practice a variety of tests are often used by the development community.

11.2 Sensitivity analysis is a fairly simplistic approach to testing viability. In essence, uncertainties can be identified in respect of the inputs and their effects can then be looked at in terms of the development return and then the level of planning payment. In short, this is a straightforward deterministic approach from which a judgement needs to be made as to the appropriateness of the outcome. Benchmarks can be used as performance measures. We have set out above at paragraph 4.20, what we consider to be an appropriate return for the Scheme in both a present day and growth context.

11.3 From our preliminary conclusions of the previous sections of this report in reviewing DS2's FVAs and supporting documentation, we considered that it was necessary to amend the DS2 appraisal having regard to the Final Offer, the results of which are presented in Tables 24 and 29 above. It is now correct to undertake sensitivity analyses in order to test the robustness of the Scheme appraisal having regard to input variance. This is also in accordance with GN 94/2012.

11.4 In light of the adjustments, in formulating a judgment, based upon this analysis we have reflected the Final Offer.

11.5 It follows that in considering the robustness of the Scheme appraisal we have looked at certain key inputs, on both a present day and growth model basis, as follows:-

I. Residential sales values; and

II. Construction costs as identified within G&T's Budget Estimate.

11.6 It should also be noted that improvements will occur as a scheme progresses in terms of efficiencies in floor area, materials, timeframes, fixing costs, etc. It is therefore useful to understand variances in inputs in order to formulate a judgement on the overall viability of the Scheme.

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11.7 Clearly the Scheme is sensitive to both cost and sales value movement in terms of viability.

11.8 Whilst there is a potential downside, we believe the market for the units given their situation, location and nature is towards the upside.

11.9 On the basis of the adjustments set out in this report, and the information provided by the JV Applicant, we are of the view the Scheme can afford the Final Offer in the form agreed in the draft S106 heads of terms.

12. Review Mechanism

12.1 There is clear separation in terms of the benefit flowing from the base position and that of the review mechanism, in how LBH and LBTH would wish to receive their proportion of surplus, if any, arising i.e. through a PIL and on-site affordable housing respectively. DS2 have stated, notwithstanding this principle, that the residential tower blocks (A & B) within the LBH are not suitable for affordable housing for design and opportunity cost reasons.

12.2 [redacted]

12.3 [redacted]

12.4 In overall terms, a review of the entirety of the Scheme prior to individual phases could work, albeit this may not fully reflect the risk that the Applicant incurred on phases completed. That said, the Applicant appears prepared to accept that position. A Convoy's Wharf type of review mechanism adapted to the circumstances of the planning application may therefore be appropriate in this instance (i.e. following a mid-point review approach in terms of the overall assessment). This would take some of the pressure off the base position in the absence of shorter term reviews as currently proposed by the Applicants.

12.5 It is essential that a financial model is set up to test both the base position and implications of the review provisions as they are worked through. This should be run on both a present day and growth basis with sensitivity analysis whilst acting as a basis for reconciliation of the offer made by the Applicants.

13. Conclusions and Recommendations

13.1 We have undertaken a detailed assessment of the material submitted.

13.2 We are of the view that the DS2 Site Value is more in accordance with the requirements of the PPG and therefore the competitive return to the willing seller of land than the suggested EUV of BNPP.

13.3 A review of comparable evidence has demonstrated that the Site Value is within the range of the market norm and we consider the assumption put forward by DS2 is reasonable, given both its analysis and our analysis of other land transactions.

13.4 Both consultants agree that the IRR is the most appropriate measure of viability. DS2 considers an appropriate target return for the Scheme to be 20% on a present day approach and 25% assuming a growth approach. BNPP consider an appropriate range for a present day approach should be between 12% and 14%.

13.5 Given the length of the development programme, and the phased delivery profile we are of the view that measuring the Scheme on the basis of an IRR is a good representation for the viability for the Scheme. Importantly the IRR takes into consideration the time value of money.

13.6 We consider the minimum target rate of return on a growth basis to be an IRR of 20% which is risk adjusted relative to the characteristics of delivering the Scheme.

13.7 [redacted]

13.8 It is our view that the Site Value reflects the value of the Site, and disregards the costs associated with the East London Line Extension Works and Suburban Line Tunnel Upgrade.

13.9 We are satisfied that the construction programme assumptions put forward by DS2 and the JV Applicant are reasonable.

13.10 In view of the magnitude of the Scheme and the timeframe over which it is to be delivered, we consider it necessary to reflect anticipated future movements in both costs and values in order to understand the outturn approach to viability.

13.11 Our role in reviewing the viability of the Scheme is to review the overall level of the Final Offer. We are not instructed to identify what costs should be apportioned to S106 items, rather we comment and conclude as to whether the overall "pot" which has been offered by the JV Applicant and the level of contribution is the maximum reasonable that the Scheme can afford, having regard to planning policy.

13.12 We currently remain of the view that the mechanism within the Convoy's Wharf Section 106 Agreement should form the basis, albeit with certain modifications, should be contained within a S106.