

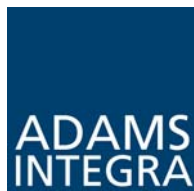
**Test Valley Borough Council**



**Affordable Housing  
Development Viability Study**

**December 2004**

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## EXECUTIVE SUMMARY

- Using residual land value techniques this report considers the likely impact of currently proposed development plan policy revisions covering affordable housing requirements, on residential development viability. It concentrates on the smaller sites which would be captured by the proposals to bring the urban site threshold down from 25 to 6 units, and the rural threshold from 15 units to 3.
- Policy proposals for the rural areas, a priority for increased site capture under the Government's Rural Agenda, are unlikely to adversely affect development activity.
- The policy proposals on the collection of financial contributions in respect of each dwelling constructed below the threshold appears to be viable in principle, but it is recommended that a range of values is used to better represent the values in each area and for varying dwelling types.
- Overall, it is felt that the findings show sufficient justification to view the revised affordable housing requirements as clear background targets to be met unless clear information demonstrates they cannot be. Hence, the policy perhaps ought to be expressed as a "baseline" against which negotiation will take place, rather than being framed in terms of minimum levels of affordable housing that are to be achieved.
- Development viability is likely to be affected in all cases of the notional development schemes trialled as representative of typical schemes coming forward in Romsey, Andover and rural areas.
- How critical this effect is likely to be in land supply terms is debateable in respect of some areas, however the results for Andover in particular give cause for concern on development viability grounds.
- Likely impacts in other areas are not thought to be so critical but viability will be affected.
- Practical application of affordable housing policy is a key recommendation – extending to consideration of available subsidy, practical and market dictated as well as financial development implications, tenure mix, potential use of off-site provision approaches.

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## 1. INTRODUCTION

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### 1.1 Background

- 1.1.1 Test Valley Borough Council's proposed planning policy (policy ESN 04 of the Test Valley Borough Local Plan Review: Revised Deposit Draft 2004) on affordable housing states:

*"Affordable housing in settlements: On sites of 6 or more dwellings (or sites of 0.2 hectares or more) within or on the edge of settlements with a population of 3,000 or more; and 3 dwellings or more (or sites of 0.1 hectares or more) within or on the edge of settlements in the rural area with a population of less than 3,000; provision should be made on site for: A) 30% of the dwellings for subsidised housing; and B) on sites of more than 10 dwellings (or sites of 0.3 hectares or more) 10% of the dwellings for discounted market housing for sale...[and] on sites below the threshold a contribution of provision off site will be sought."*

- 1.1.2 Policy ESN 04 will supersede the Council's adopted policy as outlined below:

- 1.1.3 Test Valley Borough Council's adopted policy on affordable housing states in the Revised Interim Policy H9A: Affordable Housing within urban areas:

*"To contribute to a Borough target for affordable dwellings on housing sites of:*

- a) 25 or more dwellings or housing sites of 1 hectare or more within or on the edge of settlements with a population of 3,000 or more; and*
- b) 15 or more dwellings or housing sites of 0.5 hectare or more within or on the edge of settlements in rural areas of less than 3,000 dwellings*

*25% of the developable land or plots (after allowing for site and planning policy constraints) will be used for publicly subsidised affordable housing and, subject to negotiations in relation to any specific site or local market considerations, 5% shared ownership housing"*

- 1.1.4 Objections have been made to policy ESN 04 which will be considered at a public local inquiry into the plan proposals.

- 1.1.5 For this reason Test Valley Borough Council have instructed Adams Integra Limited to carry out a study on the likely impact of affordable housing on the viability of residential development on a range of sites across the Borough, in order to determine whether land supply for residential development is likely to be adversely affected by the policy proposals.

- 1.1.6 The Test Valley Borough Council brief requests that financial assessment is carried out on the costs and values of developing sites for housing according to Policy ESN 04.

- 1.1.7 The aim of the study is to determine whether an increased proportion of affordable housing and lowered trigger threshold will significantly reduce the viability of development on smaller residential sites in particular, and whether

profitable development can be maintained without a reduction in small sites coming forward for development.

- 1.1.8 This report concentrates on those sites affected by the proposed policy changes and so are small in nature (at or close to the proposed thresholds).
- 1.1.9 In considering the options for providing affordable housing on smaller housing sites it is first necessary to determine what effect the reduced thresholds and proportions may have on the value of potential development sites. This has been carried out through the use of appraisal modelling on various areas within the Borough of Test Valley.
- 1.1.10 The modelling uses examples of different development sizes across the Borough, based on what were agreed with the Council to be typical development scenarios, to assess the effect of lowered thresholds and increased proportions on residual land values in different localities.
- 1.1.11 We use residual land value as received by the landowner as the key output of the modelling and have fixed the developer's profit throughout the modelling. The reasoning here is that land value is the key driver at the commencement of development activity and as such, unless an appropriate land value is produced, schemes do not progress (see Methodology and Assumptions for in depth discussion on this and other aspects of the modelling).
- 1.1.12 In practice successful development activity depends on many factors including an active market for the end product and a sufficient developer's profit. However by fixing the developer's gross profit at what we consider to be the minimum acceptable level, at the same time as fixing other assumptions on development cost, we are appraising viability at the margins and can study the impact on land value of varying planning led requirements – on this occasion affordable housing.
- 1.1.13 Using the same approach it is also possible to fix land values alongside other development cost assumptions, to determine the effects of changing requirements on developer's profit. However in practice the developer will fix a minimum profit level which he will need to be confident of achieving in order to pursue a scheme. In addition the use of fixed land values cannot reflect any one landowner's position or aspirations, or existing use value of a site. All sites and the circumstances surrounding them will be different and comparing land values between one site and another can be unreliable. For these reasons we do not refer to the output of developer's profit in this exercise.
- 1.1.14 We use the impact of varying affordable housing requirements on residual land value as our measure in putting forward our judgements and guidelines. With reference to the small sites studied (with the policy proposals aimed at increasing site capture as well as percentage provision), this means comparing the impact of proposed policy changes with the current position, ie where no affordable housing would be provided on these sites.

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## **2. METHODOLOGY AND ASSUMPTIONS**

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### **2.1 Introduction**

- 2.1.1 This study investigates the impact of increasing the proportion of affordable housing and reducing the threshold on the market viability of relatively small residential development sites in Test Valley Borough.
- 2.1.2 In considering the options for providing affordable housing on small housing sites it has first been necessary to determine what effect reduced thresholds and increased proportions may have on the value of a potential development site.
- 2.1.3 This report concentrates on development sites of 12 and 6 units in the larger settlement areas (population greater than 3,000) of Andover and Romsey and 3 units in the rural areas (population of less than 3,000) as agreed with Test Valley Borough Council.
- 2.1.4 The proposed trigger thresholds for on-site affordable housing are 6 units in the urban areas and 3 in the rural areas. The schemes are not in themselves actual developments but reflect scenarios that best match the policy requirements of the Council in terms of this study. However, research into local property prices in each area was undertaken to produce realistic sales and therefore development values for each appraisal model (see Model Areas below).
- 2.1.5 The size of the development sites was agreed as best representing development at the margins of the proposed policy, and of a type typically coming forward in the various localities. A six unit scheme in the larger settlements allows us to model the effects of a policy of 30% subsidised housing requirement whereas the 12 unit scheme allows us to model the 30% subsidised plus 10% discounted market housing policy (the additional 10% being triggered at 10 units or more). In the rural areas a three unit scheme again allows us to test the viability at the margins of a 30% subsidised housing policy.
- 2.1.6 In addition to the above model scenarios, Adams Integra has been asked to consider the effect of the proposed policy on a notional 15 unit scheme, in order to illustrate the difference between current PPG3 policy and the proposed Test Valley Borough Council Policy ESN 04.
- 2.1.7 Finally, Adams Integra, at the request of Test Valley Borough Council, has also modelled an off-site contribution scenario for those sites that fall below the threshold in the rural areas (e.g. 2 units notional scheme) and in the larger settlement areas of Andover and Romsey (e.g. 5 units notional scheme). The Council's policy proposals include the collection of a financial contribution to affordable housing need in respect of every dwelling built on sites beneath the respective proposed threshold levels.
- 2.1.8 Developer's profit and landowner's sale price are key considerations that must be taken into account if residential development is to be undertaken. If profit levels fall below a certain level then developers will not take the risk of developing a site nor will funding organisations lend them the finance to develop. Equally, if the

price offered by a developer to a landowner for a site is too low, the landowner may not sell and instead continue with, or pursue, an existing or higher value use. There are also intangibles, for instance some of the sites we are considering here will start out as peoples' homes or gardens which will not be sold unless certain aspirations are met. Part of Test Valley Borough Council's policy on negotiation of affordable housing is to investigate the existing use value of a site compared to the potential uplift from new residential development.

- 2.1.9 The requirement to place a proportion of affordable housing on a site will inevitably reduce the sales revenue that a developer can reasonably expect to receive. As this reduction will not be accompanied by lower construction costs, the offset must be taken up in either a reduced development profit, lower land price or a combination of the two.
- 2.1.10 Assuming that a developer will require a minimum fixed profit margin on any given site to balance risk and obtain funding, beyond a certain point it is therefore the land value that will be affected by the introduction of affordable housing or other infrastructure requirements, provided the developer's profit expectations are not excessive.
- 2.1.11 To establish the potential effect of affordable housing on the supply and development of relatively small housing sites, it is necessary to compare a site that does not include an affordable housing element (adopted policy at the thresholds being considered) with that which will be subject to the proposed policy within the Local Plan Review: Revised Deposit Draft 2004.

## **2.2 Approximate Residual Land Value**

- 2.2.1 In order to determine the impact of proposed affordable housing policy on a range of site types and locations it is necessary to determine a common indicator.
- 2.2.2 In normal circumstances the developer is aiming to secure a predetermined level of profit. From a developer's point of view and assuming a conclusion is reached that a site is viable for development, an appraisal is carried out to discover what sum a developer can afford to pay for the site. Some sites coming forward will have been owned for considerable periods and those will have to be dealt with case by case, however we have to assume that a negotiation has occurred or is under way based on knowledge of the current development climate and policy requirements.
- 2.2.3 The most effective way of checking site viability is via a developer-type residual land value model. We have developed our own spreadsheet model for this purpose. In doing so we have made what we feel are reasonable assumptions but it must be noted that individual developers will have their own variety of approaches, and a developer might also apply a different approach from one site to another. A simplified example is shown below in Figure 1.

**Figure 1: Simplified Example of Gross Development Value Calculation for illustration purposes only.**

|   |                   |
|---|-------------------|
| <b>Total Sales Value</b>  |                   |
| Number of Units =   | 10                |
| Sales Value =   | £120,000          |
| <b>Gross Sales (Development) Value = A</b>  | <b>£1,200,000</b> |
| <b>Development Costs (build costs, fees, etc.) = B</b>  |                   |
|   | £575,000          |
| <b>Min Development Profit (@15% of Sales Value) = C</b>   |                   |
|   | £180,000          |
| <b>Land Purchase Costs and Planning Infrastructure (not including affordable housing element) = D</b>       |                   |
|   | £75,000           |
| <b>Land Residual (Gross Sales Value - Development Costs - Profit - Land Purchase and Planning Gain) = E</b> |                   |
| <b>A – (B + C + D) = E</b>  | <b>£370,000</b>   |

- 2.2.4 This general method, however, reflects one of the main ways of how development viability tends to be assessed in the market place, and land value checked relative to sales values and development costs. Through discussion with developers we have been able to verify our experience and thoughts on components of the model and output land values, as well as the general approach.
- 2.2.5 The model used for analysis in this instance uses a calculation that provides an approximate residual land value, after taking into account assumed normal costs for site development (nb: other than broadly estimated un-complicated site clearance costs, no allowances have been made for abnormal site costs). Added on to this is the inclusion of an affordable housing element, whereby the developer receives a payment for a number of completed units based on predetermined calculation (discussed later), but that is not at a level comparable with open market values.
- 2.2.6 In addition, an allowance for other planning infrastructure costs has been made. The figures used for infrastructure payments are as a result of discussions with Test Valley Borough Council officers. The figures are shown in 2.8 – “Other Assumptions”.
- 2.2.7 The result then shows the change in approximate land value or change as a percentage of approximate gross development value. It should be noted that this is based on notional sites and is a relative exercise only - to determine the probable effect of revised policy. Therefore not too much weight should be



attached to the actual values arrived at - the changes in results as the affordable housing criteria alter are the key outcomes.

- 2.2.8 Gross development value (“GDV”) has been taken as the amount the developer ultimately receives on completion or sale of the scheme whether through open market sales alone or a combination of those and the receipt from a RSL for completed affordable housing units. Thus the developer’s profit in each case relates to that scheme specific sum rather than to a base level of GDV that assumes no affordable housing. It therefore assumes that the developer has appraised the site and secured land in the knowledge of and reflecting policy that will apply. This can be regarded as a reasonable approach given national policy guidance on the provision of affordable housing.
- 2.2.9 As policy alters, there will tend to be a hiatus in supply while previous land deals and planning consents come forward (some of those may not be able to support latest policy), but we have to envisage a period of adjustment leading to sites being appraised differently. The approach we suggest of adopting clear targets, but then being prepared to negotiate in light of site specifics should cater for the range of scenarios that the Council will need to deal with.
- 2.2.10 Ultimately, land value is a product of a series of calculations that provides a residual valuation based on what specific form of development a site can accommodate; and its development costs. While the market uses a variety of approaches, including comparisons between sites, to appraise sites and schemes, this sort of more detailed approach is necessary to understand how the value/cost relationship looks.
- 2.2.11 Adams Integra’s experience of working with a range of developers leads us to suggest that they would need to seek a fixed profit of at least 15% (gross) and probably more (depending on a number of other factors – profit expectations could be up to 25% or more) of gross development value. Only if the projections reveal this fixed profit margin (as a minimum) would they pursue a site.
- 2.2.12 This model uses a developer’s profit (gross) fixed at 15% of gross development value, which is at the lower end of the acceptable profit range in normal circumstances. Some developers will look at alternative profit criteria, for example a higher percentage (perhaps up to 30%) of capital employed. We felt it appropriate to appraise the scenarios at the margins.

### **2.3 Model Areas and Unit Values**

- 2.3.1 Following discussions with Test Valley Borough Council, it was decided that the following typical example areas would be used on which to base the model scenarios:
- Andover
  - Romsey
  - Rural Areas
- 2.3.2 The locations chosen represent a spread of property value areas and cover both urban (large settlement areas) and rural (small settlement areas).

- 2.3.3 The rural areas are unspecified and relate to rural settlements throughout Test Valley. This is primarily to ensure that the population sample for the house price data was large enough to give accurate average dwelling values of rural properties.
- 2.3.4 In carrying out this study, Adams Integra have reviewed the asking and subject to contract sale prices of over 320 one and two-bed flats and two and three-bed houses within the specified example areas to enable us to provide reasonable average values for each area. Property prices for each of the areas modelled were assembled by utilising internet property search engines. The tables and graphs relating to this exercise are shown in Appendix I. The values were verified with a number of estate agents across the Test Valley Borough. Note: the data for values of flats in rural areas were not included in the appraisals and are included in the tables and graphs for information only.
- 2.3.5 This report does not attempt to provide comprehensive property valuation data but rather provides average values of unit types within a particular area and does not allow for street by street variations. The values used in the appraisals are an average of all available properties of varying size and type and it must be remembered that any settlement will contain a range of property values covering a single property type. We believe however that the information used is representative.

## **2.4 Model Scenarios**

- 2.4.1 Test Valley Borough Council required a range of scenarios to be tested across each of the model areas reflecting the impact of differing policy proposals on site viability. These are outlined below:
- a) Andover – 15 units (5 no. 1-bed flats and 10 no. 2-bed flats); 30% subsidised and 10% discounted market;
  - b) Andover – 12 units (4 no. 1-bed flats and 8 no. 2-bed flats); 30% subsidised and 10% discounted market;
  - c) Andover – 6 units (6 no. 3-bed houses); 30% subsidised;
  - d) Romsey – 15 units (5 no. 1-bed flats and 10 no. 2-bed flats); 30% subsidised and 10% discounted market;
  - e) Romsey – 12 units (4 no. 1-bed flats and 8 no. 2-bed flats); 30% subsidised and 10% discounted market;
  - f) Romsey – 6 units (6 no. 3-bed houses); 30% subsidised;
  - g) Rural – 3 units (3 no. 3-bed houses); 30% subsidised;

In addition to the above, scenarios testing the viability of requesting commuted sums for all units on sites below the proposed threshold have been undertaken. These were carried out on notional sites of 5 units in Andover and Romsey, and 2 units in the rural areas. This then reflects the impact of such policy on sites immediately below the proposed thresholds.

- 2.4.2 The 15 and 12 unit schemes in the larger settlement areas represents a typical infill/redevelopment site which would be captured by the Council's proposed policy of 30% subsidised and 10% discounted market housing above a threshold of 10 units. These notional sites correspond to a typical flatted scheme in the town centre on brownfield land.
- 2.4.3 The 6 unit schemes represent a smaller development of townhouses, which would be captured under the Council's proposed policy of 30% subsidised housing on sites of 6 or more dwellings. We understand that these schemes are fairly typical of what developers are pursuing on small infill or ex-commercial sites.
- 2.4.4 The three unit scheme in the rural areas again represents a site which would be captured by the proposed policy which reduces the rural threshold to 3 units. We are conscious that in the rural areas in particular there is a demand for larger and detached property, and sites of that nature will need to be considered individually in term of a practical approach to application of policy (not within the scope of this report, but possibly to include the use of payment in lieu of on site provision).

## **2.5 Unit Types, Mix and Size**

- 2.5.1 For the 15 unit schemes, the envisaged development consists of a flatted scheme of 10 no. 2-bed flats and 5 no. 1-bed flats.
- 2.5.2 For the 12 unit sites, the development consists of a flatted scheme of 8 no. 2-bed flats and 4 no. 1-bed flats.
- 2.5.3 For the 6 unit sites, the envisaged development comprises 6 no. 3-bed townhouses.
- 2.5.4 For the 3 unit sites, the development consists of a terrace of 3 no. 3-bed houses.
- 2.5.5 The flat sizes used in the modelling are 51 sq m for one-bed and 61 sq m for two-bed flats. We have assumed a bias towards 2 bed flats. In practice (on a smaller site in particular) a developer might seek a totally uniform scheme. In terms of design and cost – the floor plates, service positions etc. need to marry up reasonably. Therefore a practical approach to policy application will again be necessary.
- 2.5.6 For the three-bed houses we have used 80 sq m as a representative size.
- 2.5.7 Two-bed units would tend to be more popular on the market generally, with a wider market and increased sales figures tending to encourage developers towards those in many areas. In practice there would also be a tendency towards developers needing to maintain the higher value units within a scheme for private sales whilst thinking about the relationship of the private units to the affordable units in terms of location. These are all factors which in practice (and dependent on the site location and characteristics) will affect the unit and tenure mix.

## **2.6 Affordable Housing Unit Transfer (to RSL) – Method of Payment Calculation and Type of Unit Transferred**

- 2.6.1 Discussions with Test Valley Borough Council indicate that the payments developers receive from RSLs for the provision of completed affordable units on-site effectively reflect a free land scenario. The amount a developer can expect to receive for completed units is equivalent to the reasonable build costs for the dwelling type and site conditions. We have taken what we feel is a fairly cautious view of the payment likely to be received by the developer from the RSL given the uncertain affordable housing funding climate. In practice, a developer may be able to recoup a larger sum, improving site viability marginally. However there will be costs associated with servicing the affordable housing land to its boundaries and the RSL will also need to fund its own development management cost, hence we have not allowed for the developer receiving back the equivalent of the full design and build cost. We have assumed a rate of approx £1,000/sq m (gross internal floor area of development) will be received in the case of standard house schemes, and £1,100 in the case of flatted schemes.
- 2.6.2 Within the models used for each of the scenarios listed above we have assumed that the affordable housing element of each scheme is tenure neutral. This is because by applying the assumption that the developer's receipt from the affordable housing will be build cost based, there is little difference between the costs of providing for different tenures. If sales values and the percentage share of a discounted market housing unit were increased, this may increase slightly the financial viability of some sites.
- 2.6.3 In reality each scheme will differ as it could be argued that for low cost ownership forms of tenure provided on site, the market value of the remaining private units might not be affected as much as by affordable rented tenure adjacent. As above, we have not reflected such subtleties as it is not possible to do so on notional sites where the positioning of units and accesses etc is not known. However these are real factors in the market which again it is suggested should be assessed as part of a practical approach to producing successful development schemes as a whole. As indicated in their Draft SPG on Affordable Housing, the need to achieve successful housing development in the mix of housing types, tenures and local management are important issues for Test Valley Borough Council.
- 2.6.4 These issues will again depend on the site, need, design and other factors; however as a rule and for simplicity (bearing in mind this is a relative exercise), we have assumed that the generally accepted "premium" (price addition) of say 10% for new build property over most older property (not in higher value areas – listed buildings, expensive conversions etc but compared with 20+ year old purpose built flats, and sometimes poor conversions) will be cancelled out by the on site affordable housing, particularly in the smaller developments we are considering.
- 2.6.5 This effect on values stems from a perception of affordable housing which we have to acknowledge exists and particularly affects parts of smaller sites in many purchasers' and therefore developers' thinking.

2.6.6 As this is a relative exercise we have not adjusted the sales prices from the data collected when looking at the “no affordable housing” approximate land values, as modelling that scenario was not a part of the brief and we must be careful not to overplay the impacts from affordable housing. We have considered those appraisals purely in the background to help provide a general feel for how values might look where no affordable units are provided, and therefore for a guide to the impact of affordable housing policy. In any event, site and property specifics would be different every time.

2.6.7 The modelling has been based on transferring units for affordable housing in proportion to the number of each type within the overall scheme as far as possible. For example in a scheme of eight 2-bed units and four 1-bed units, the subsidised and discounted market element would be three 2-bed units and one 1-bed unit. This approach reflects the likely range of affordable housing need in most locations, but again in practice site specific discussions would prevail.

## **2.7 Payment by Developer**

2.7.1 The Council’s proposed policy requiring a financial contribution to affordable housing needs to be made for all units below the proposed thresholds has also been modelled as stated above. In these cases, the payment made by a developer is calculated from Test Valley Borough Council’s current Draft “Financial Contribution for Sites Below the Threshold” document and included in the original SPG on affordable housing. Should the payment calculations change, this will affect the result of the viability model.

2.7.2 The document states that “Sites below the proposed threshold will make a significant contribution to the overall supply of affordable housing in the Plan period. To support the provision of affordable housing a financial contribution will be sought from such sites...In order to provide an equitable approach to the affordable housing provision requirement on site, the financial contribution required will be based on a pro-rata equivalent of the cost of providing serviced land free of charge. A 30% requirement is made as this is the requirement for sites under 10 units:

$$\textit{Current serviced land price per plot} \times 30\% = \textit{per unit contribution}”$$

2.7.3 This contribution is given as equating to £15,600 per plot for sites below the threshold (30% of £52,000 which is the 2004/05 valuation for serviced land per plot.

## **2.8 Other Assumptions**

2.8.1 The appraisal model includes other variables such as fees, land buying costs, finance, agency costs and planning infrastructure provision that are all taken into account when calculating an approximate land residual value.

2.8.2 These figures in some instances are factors of other elements of the appraisal and therefore vary by site size and type. In practice each site and developer approach would vary and it is appreciated that the figures used here will not always be appropriate, but this enables a comparison to be drawn across sites on a ‘like for like’ basis.

2.8.3 The percentages and values assumed for the purposes of this exercise are listed below and are the result of Adams Integra experience and discussions with developers:

- **Build Costs (House Schemes) – £1,000 / sq m**
- **Build Costs (Flatted Schemes) - £1,100 / sq m**  
Base costs are likely to be higher than for a scheme of houses particularly for small flatted schemes where sites are small and often difficult to work on (storage, craning etc), and where the sub-contractor and labour market is relatively stretched owing to level of demand.

Typical scheme specific additions to these are:

- **Demolition/Site Clearance – £25,000** for all urban schemes. It has been assumed that development is likely to take place on brownfield / infill sites in the large settlement areas with at least a degree of site clearance. A cost has thus been added to each appraisal to take this into account. These values are based on our best estimates for an uncomplicated small site clearance with no contamination or deleterious materials. Please note that we have made no allowance for Party Wall complications or works in this appraisal. No site clearance costs have been allowed for in the rural, small settlement areas.
- **Architect Fees** 3.5% of build costs
- **Engineer Fees** 1.5% of build costs
- **Contingencies** 5.0% of build costs
- **Insurances** 2.5% of build costs
- **Selling Agents Fees** 1.5% of Estimated Gross Sales Value
- **Legal Fees on Sale** £1000 per unit
- **Finance (build)** 6.0% APR on above costs over 52 weeks for urban area schemes; 26 weeks for rural areas
- **Land Survey Costs** £3,000 per site for the rural areas, £5,000 per site for the urban areas (including ground conditions research)
- **Legal Fees on Land Purchase** 0.5% of land value (this will often produce a low figure (when looking at very small or low value sites) but only make a minimal difference to outcome.
- **Planning Application costs** £220 per unit
- **Stamp Duty** Between 0% and 4% depending on residual land value

- **Infrastructure Payments** *£variable per unit* (applied in all cases, regardless of site specifics). Test Valley Borough Council negotiates infrastructure payments on each site individually and for items such as outdoor recreation space provision negotiations are based on probable occupancy rates. Following discussions with Test Valley Borough Council a series of calculations was produced to achieve an approximate overall value for infrastructure payments. These figures in reality would be based on site specific circumstances and so these payments used are an approximation. Figures used in the appraisal are as follows:
  - Non – Rural Off Site Open Space - £814.51 per person\*
  - Non-Rural On-Site Provision – if provision not met on site a payment would be required of £11,426\*/ \*<sup>1</sup>
  - Rural Off Site Open Space (Pitches only) - £594.85 per person\*
  - Rural On-Site Provision – if provision not met on site a payment would be required of £5,713.12\*<sup>1</sup>
  - Primary Education - £1,844 per dwelling unit\*<sup>2</sup>
  - Secondary Education - £1,928 per dwelling unit\*<sup>2</sup>
  - Highways – no contribution used in these appraisals as in reality would be based on layout and individual characteristics of the site.

\* Children’s play space contribution not expected from 1-bed units

\*<sup>1</sup> Assumption has been made that contribution in-lieu of on-site provision will be made although this will necessarily depend on site constraints.

\*<sup>2</sup> Education contributions not sought from affordable element or 1-bed units in this appraisal.

Please note that these are the figures used in the appraisals but are not necessarily representative across all new residential developments as each site will be calculated separately.

- **Finance related to land purchase** *6.0% APR* on land survey, planning costs, legal fees on land purchase and residual land value over build time plus 26 weeks. No finance arrangement fee has been included for the purposes of this exercise as we are appraising small schemes. As with much of this exercise, this is a snapshot as it appears that rates are moving upwards and over time we would need to see how added costs balanced with what sales values were doing.

2.8.4 As this is a relative exercise aimed at determining the likely effect of the Council’s proposed policy position, the most important factor is consistency between assumptions used for modelling scenarios. As we point out, specific assumptions

and values for our notional schemes may not be appropriate for any particular actual development.



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## **3. RESULTS ANALYSIS**

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### **3.1 Introduction**

- 3.1.1 The results of our modelling are shown in Appendix II. Table 3 shows the reduction in residual land value as a consequence of lowering thresholds and increasing the proportion of affordable housing required. Table 3 is modelled on the basis of transferring completed affordable units to an RSL in return for reasonable build costs.
- 3.1.2 Table 4 shows the reduction in approximate residual land value on sites below the proposed policy thresholds where financial contributions are proposed on a per unit basis according to a 30% share of the prescribed notional plot value.
- 3.1.3 The results have also been represented in a series of graphs (4 to 6) which are sourced from Table 3. Graph 4 shows the percentage reduction in residual land value from existing (no affordable housing) to proposed policy in each of the model areas and across the range of schemes. Graph 5 shows the approximate land residual for each of the areas and compares the effect of proposed policy with existing. Graph 6 shows the approximate land residual as a percentage of gross development value across the same areas.
- 3.1.4 Graphs 7 - 9 (sourced from Table 4) show the same information as graphs 4 - 6 but reflect the Council's proposed policies on financial contributions below the proposed threshold levels.

### **3.2 Reduction in Land Residual**

- 3.2.1 Analysis of the results indicates that, as expected, increasing the affordable housing requirement and reducing the thresholds on the scenarios modelled leads to a reduction in residual land value.
- 3.2.2 A comparison of the reduction in land residual values in Table 3 (column 9) resulting from a proposed policy of 30% subsidised and 10% discounted market housing on sites with 10 or more units indicates a reduction of approximately 92.6% for a 15 unit scheme in Andover and 61.0% for a 15 unit scheme in Romsey. For a 12 unit scheme we see an approximate reduction of 80.9% and 52.4% in Andover and Romsey respectively.
- 3.2.3 On sites of six or more units, where Test Valley Borough Council's proposed policy expects 30% of units to be affordable (subsidised), the reduction in land residual is less than the results discussed above. In Andover the reduction is approximately 61.2% and in Romsey the reduction is approximately 50.5%.
- 3.2.4 When looking at the rural scenario, the likely impact of the policy proposals is smaller and a lower reduction in land residual of approximately 39.0% can be seen.

### **3.3 Land Residual (as a percentage of GDV) – Tables 1 and 2, Column 8**

- 3.3.1 While 3.2 above highlights the impact of affordable housing on site viability by looking at the overall reduction in land residual value, it is also relevant to review the approximate land residual figures produced (in monetary terms) and compare these across the range of proportion and threshold levels considered.
- 3.3.2 These are notional/illustrative only and not too much weight should be attached to them, but what we attempt to do is get a general feel for the amounts of money likely to be available to landowners, to help assess to what extent they might be incentivised to sell. There can be no definite cut off point, as discussed above for example at 2.1.8., owing to each landowner's position. It is not appropriate to assume that because a development appears to produce some land value, the land will change hands and the development proceed. This must be viewed alongside the owner's enjoyment/use of the land and other options available to them. This is highlighted by Test Valley Borough Council's policy on negotiation of affordable housing as indicated in 2.1.8.
- 3.3.3 As stated above, for background and general comparison the modelling has investigated the residual land value with zero affordable housing to determine the approximate land value if the revised planning policy proposals promoting affordable housing on smaller sites did not apply. That reflects the current position in relation to the smaller sites, which would be captured by the proposed thresholds.
- 3.3.4 Appraisals have also been carried out on by modelling a scenario of 15 units to reflect the lower limit of current Government policy for comparison purposes.
- 3.3.5 In terms of the approximate land residual remaining for the 15 unit schemes (columns 7 and 8 of Table 3), Andover shows approximate land residual lowering from £277,940 to £20,433 (or from 14.8% of GDV to 1.4% of GDV) as a result of the proposed policy. For a 12 unit scheme, the land residual is reduced to a slightly lesser extent – from £216,532 to £41,383 (or from 14.4% to 3.3% of GDV).
- 3.3.6 A similar pattern is seen in Romsey, the land residual drops from £679,166 to £265,001 (or from 27.9% to 14.4% of GDV) for a 15 unit scheme. Again the effect of proposed policy on a 12 unit scheme is slightly less with approximate land residual lowering from £537,573 to £255,667 (or from 27.6% to 16.6% of GDV).
- 3.3.7 It must be noted that the reduced impact of the 12 unit scheme is as a result of the fact that 40% subsidised/discounted market housing equates to 4.8 units and as such only 4 units are requested to be provided on site. With a 15 unit scheme, 40% equates to exactly 6 units and as such this has the effect of reducing the viability further than on a 12 unit scheme as an extra two affordable units are required but with only an additional three units in total. This misleadingly skews the figures in favour of a 12 unit scheme; consequently these figures must be viewed in context.
- 3.3.8 For the 6 unit schemes Andover shows approximate land residual lowering from £235,923 to £91,513 (or from 22.0% of GDV to 10.5% of GDV). In Romsey, the

approximate land residual drops from £355,237 to £175,938 (or from 28.8% to 17.9% of GDV).

- 3.3.9 For the rural scenario and a three unit scheme, the approximate land residual drops from approximately £402,261 to £245,323 (or from 45.0% of GDV to 36.3% of GDV).
- 3.3.10 These figures show that there are varying differences across the range of value areas modelled in terms of reduction in residual land value resulting from the proposed policy of 30% subsidised and 10% discounted market housing for the larger sites and the proposed policy of 30% subsidised housing for the smaller sites.
- 3.3.11 These results also show that the impact of the proposed policy is to significantly reduce the land residual across all three model areas. In the rural areas and to some extent Romsey, the impact is dampened by higher sales values (see Appendix I) widening the gap between development value and costs. However, in Andover, where residential values are significantly lower, the impact is considerable with absolute figures showing near zero land value on the 15 and 12 unit schemes taking into account the affordable housing policy proposals.

#### **3.4 Payments below the Threshold**

- 3.4.1 Test Valley Borough Council also requested that a scenario reflecting their proposed policy on financial contributions for sites below the threshold be tested.
- 3.4.2 Table 4 and graphs 7 – 9 show the results of this modelling. A similar pattern emerges to that above in that the greatest impact of the policy is seen in the Andover model area where the property prices are at their lowest. Table 4, column 9 shows that in Andover, the reduction in residual land value as a result of the proposed policy is approximately 31.0%. In Romsey this reduces to approximately 18.6% and in the rural model areas this figure is lower still at 7.2%.
- 3.4.3 In terms of the actual land residual values this equates in Andover to £197,898 following current adopted policy where no payment is requested and £136,528 following proposed policy where a fixed payment per unit is requested (see above for payment details).
- 3.4.4 In Romsey the figures are £297,300 and £242,059 for adopted and proposed policy.
- 3.4.5 In the rural model areas the residual land values are £265,357 and £246,280 for adopted and proposed policy respectively.

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## 4. Conclusions

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- 4.1.1 Test Valley Borough Council's brief set out to determine whether viable residential development on smaller sites could be maintained as a result of reducing the current thresholds and increasing the proportions of affordable housing across the Borough.
- 4.1.2 The results highlighted above and shown in Table 3 and the associated graphs indicate, as expected, that the proposed threshold reductions and increase in proportions of affordable housing sought on qualifying sites has a variable impact across the model areas. In all cases though, the proposed policy has the effect of reducing the residual land value, and often significantly.
- 4.1.3 The greatest impact is seen in the Andover model area and from this it is possible to extrapolate the results to reflect all areas in the Borough with similar residential property values. The impact is less in Romsey and the rural areas and again the same results would be seen in other areas within the Borough with comparable property values.
- 4.1.4 In terms of proposed policy it appears that the higher value rural areas of Test Valley may be able to sustain the proposed policy changes. Although the impact is marked and the approximate residual land values are reduced, they still remain *relatively* strong in terms of encouraging land supply.
- 4.1.5 In Romsey, although significantly better than Andover, the residual land values are still relatively low and quite possibly on the margins of viability.
- 4.1.6 The large reduction in residual land values in the Andover area as a result of the proposed policy introduction gives some cause for concern. The results above indicate that the introduction of proposed policy in areas such as Andover could have a significant negative impact on the supply of residential land, and thus fail to meet the aims of the policy i.e. the provision of greater numbers of affordable housing units. It needs to be remembered that values for residential development must be sufficient relative to existing or alternative use values (e.g. commercial/domestic) for residential schemes to be pursued and promoted. This statement is likely to be particularly relevant in more urban than rural development situations.
- 4.1.7 There are no simple rules as to the relationship between residential and alternative land use values. However, in terms of incentives to consider residential use over other uses, for example non-conforming use in a residential area, there will tend to be more consistency between commercial values in different areas. This can mean there being a far greater difference between existing/alternative use value in a high value residential area than in a cheaper housing area such as Andover where low residential development values may be particularly unhelpful in terms of encouraging the release of sites given the attractiveness of alternative use values. Test Valley Borough Council outline policy to address this situation by encouraging the investigation of existing use values of sites compared to values created by new residential development to verify the viability of new development. In tandem with this, Test Valley Borough Council also encourage an "open book" approach by developers to ensure that developer's concerns over viability can be addressed if necessary.

- 4.1.8 What the above illustrates is that in the lower value areas particularly, schemes may need assistance through a flexible application of policy. Although introducing separate policies for different areas would alleviate some of the impact of the proposals (i.e. higher thresholds/lower proportions in Andover and similar areas) it would not be practical. It is therefore important to ensure that flexibility in approach to policy is maintained through Test Valley Borough Council's proposed policies on affordable housing.
- 4.1.9 With regard to the rural model areas and Romsey, there will be instances where location, design, servicing cost, marketing or other practical issues will mean that a reduced proportion of less than 30 - 40% affordable housing (dependent on the threshold) will need to be negotiated following open discussions with developers.
- 4.1.10 There will also be cases where the development value/cost relationship will not be strong enough to support a high proportion of affordable housing and we are unable to state categorically that the proposed policy will be achievable across the board. There is no one "cut-off" point where sites become unviable; each needs to be considered given its specific characteristics.
- 4.1.11 The proposed policy requires a minimum proportion of affordable housing i.e. "the Council will expect a minimum of 40% of housing on sites above the size thresholds to be affordable". It is suggested that greater flexibility could be attained by viewing the 40% as a "baseline" (or 30% in the lower threshold sites), on the basis that developers needed to prove why particular targets could not be met if that were the case. This would then allow the Council manoeuvrability when negotiating on sites in the lower value areas such as Andover and may help viability in Romsey and similar areas. In whatever form, it is important that the Council sets a clear "baseline" against which a negotiated approach based on site specifics could be adopted. This approach is one advocated by the Government guidance such as c.6/98 and PPG 3, and is an approach likely to be confirmed and strengthened as that guidance is reviewed.
- 4.1.12 In terms of per unit financial contributions for sites below the proposed thresholds, the payment mechanism appears to work in principle in all model areas. Again however in Andover, the land residual (and thus viability) is affected to a greater degree as a result of lower residential property values. Once again, a flexible approach to the application of this proposed policy would be recommended to ensure site viability is maintained and land supply continues.
- 4.1.13 Broadly, the contributions policy appears potentially workable in most areas, and this element of proposed policy has the potential to produce very useful additional funds without unduly compromising many of these smaller sites. However, the proposed policy at present does not allow for differences in land value or property types across the Borough. It is therefore recommended that a range of values are used that link to specific areas and dwelling types.
- 4.1.14 Clear policy, targets and Supplementary Planning Guidance will ultimately help with land value expectations and site delivery. The severest problems will come on those sites which have already changed hands or are committed through option or similar arrangements where figures may simply not work when set against the proposed policy requirements. Any SPG needs to be capable of being

updated readily, a process that may be made easier by the introduction of the Local Development Framework arrangements.

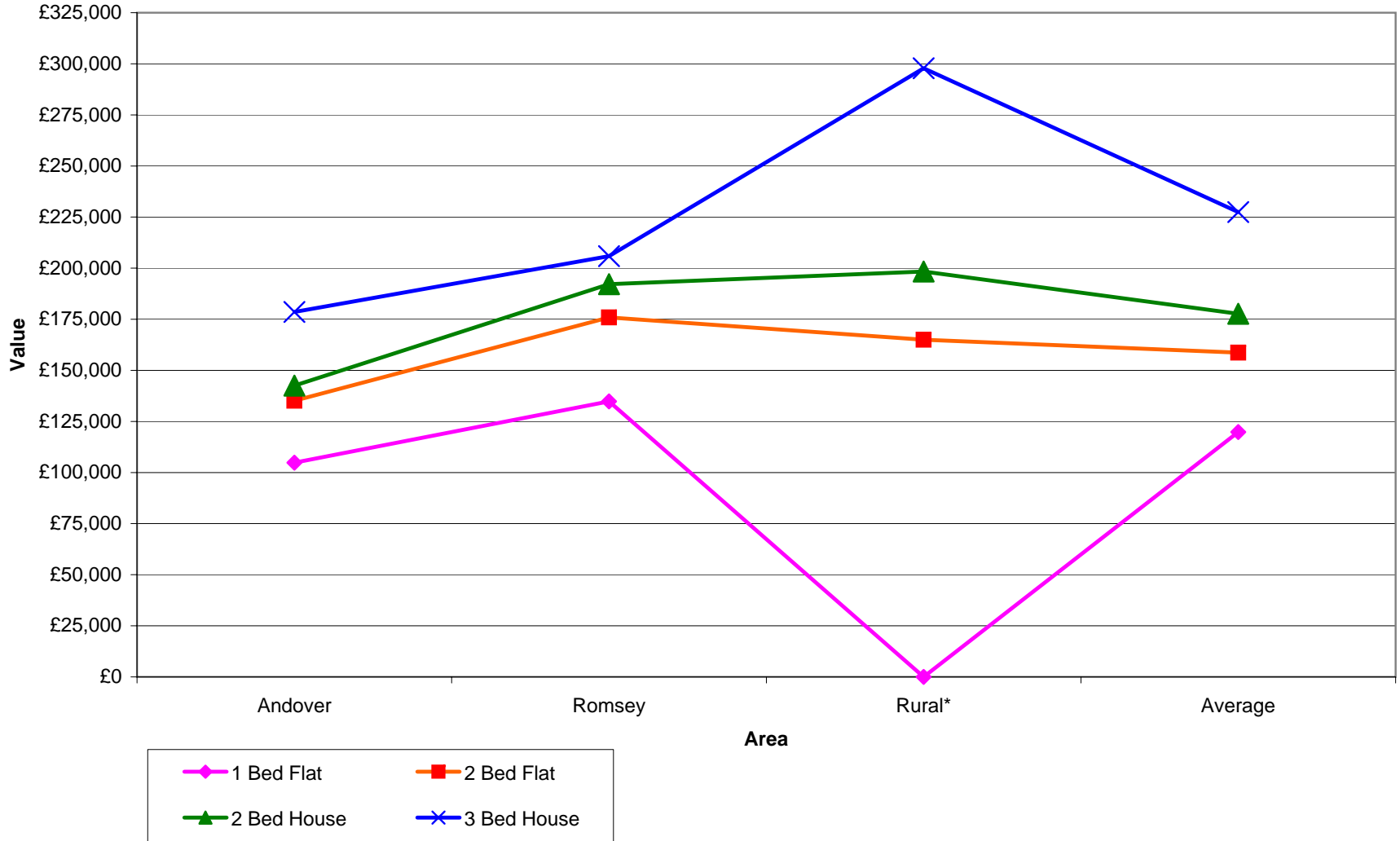
End of Main Report  
Appendices follow  
**December 2004**

## **APPENDICES**

**Appendix 1 - House Price Data**

**Appendix 2 - Results of Land Residual Calculations (Tables 3 & 4; Graphs 4 - 9)**

Graph 1: House Price Comparison Across the Test Valley



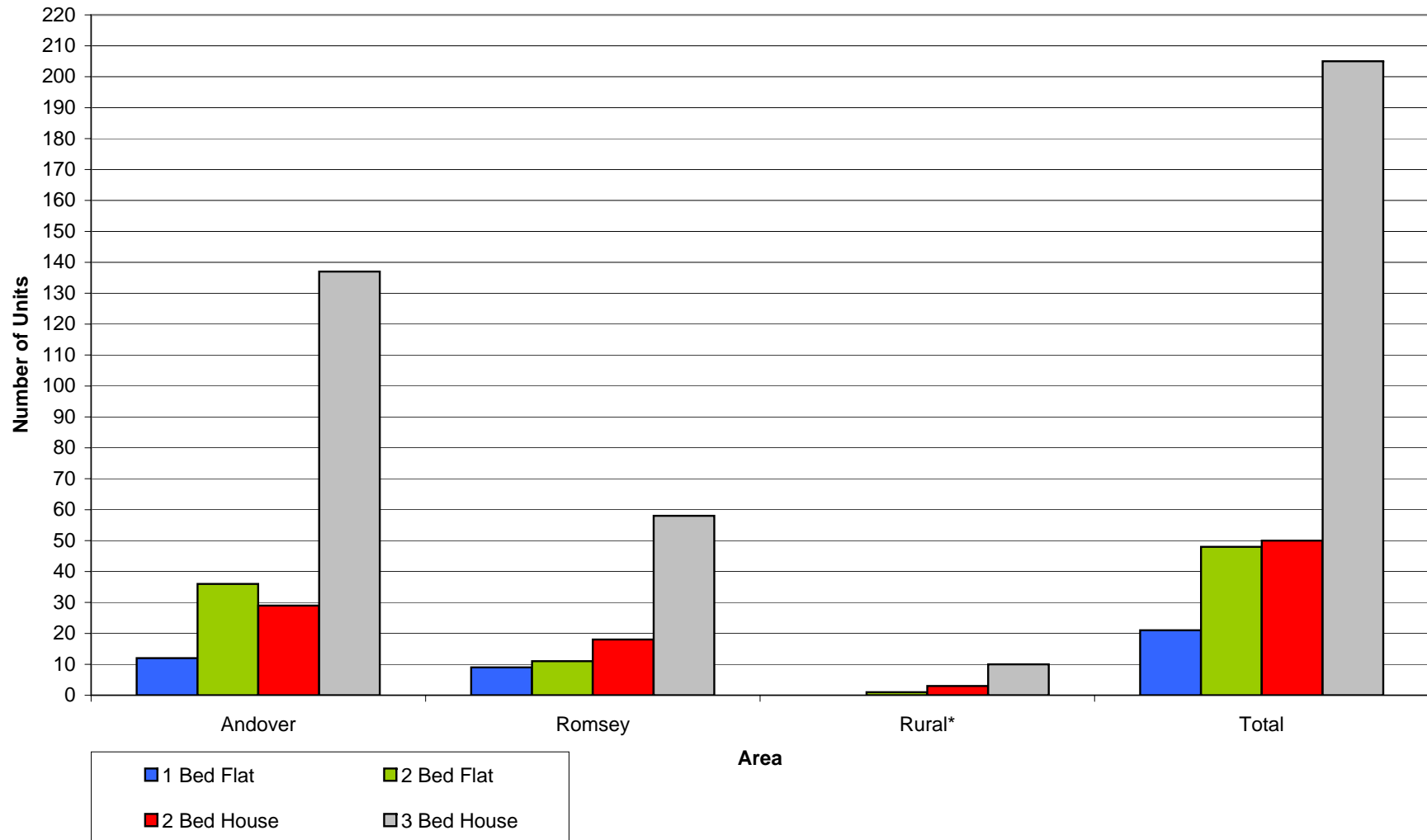


**Table1: House Price Data for Test Valley**

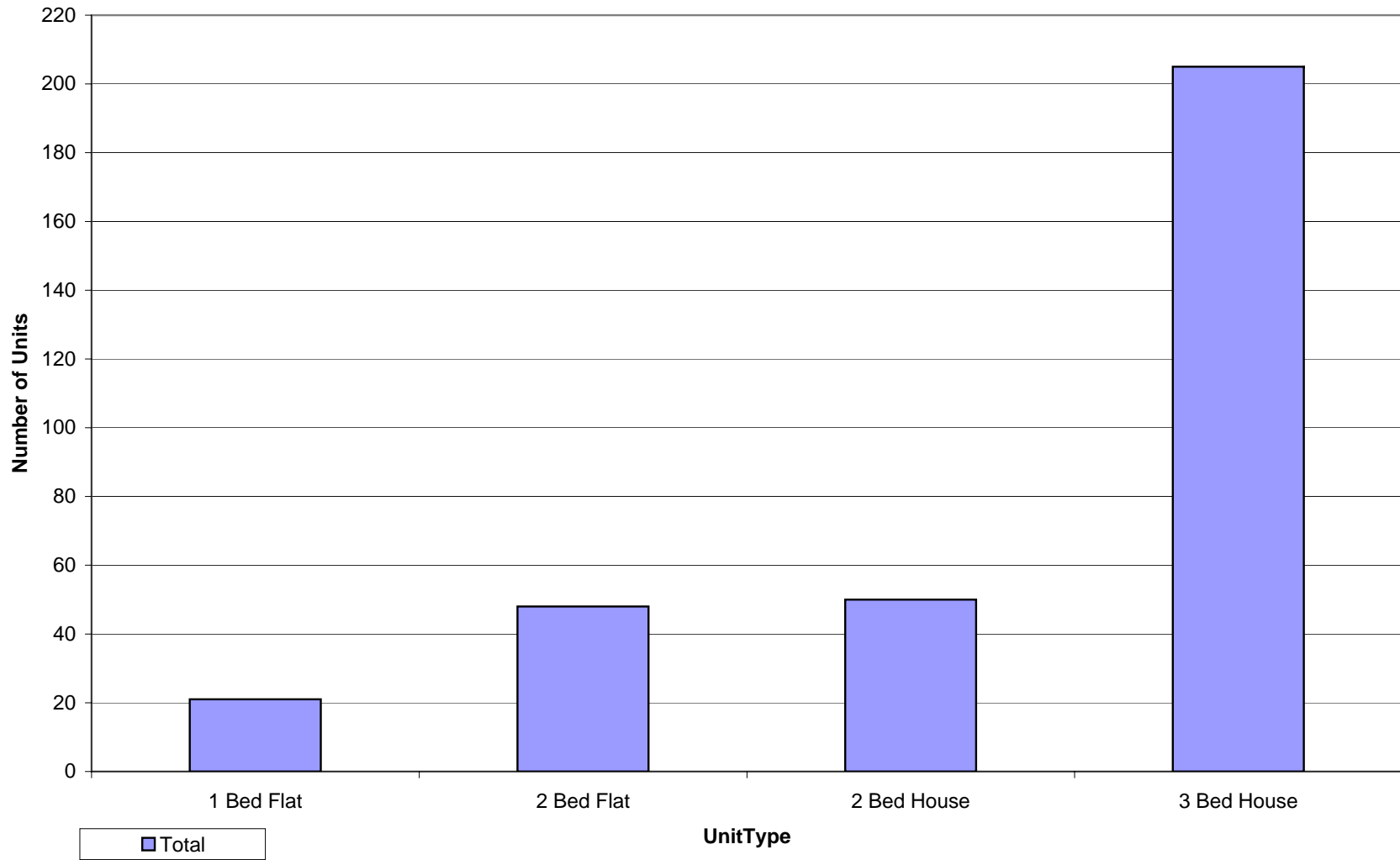
| Area           | Dwelling Type   |                 |                 |                 |                 |
|----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
|                | 1 Bed Flat      | 2 Bed Flat      | 2 Bed House     | 3 Bed House     | All             |
| Andover        | £104,845        | £135,101        | £142,503        | £178,576        | <b>£140,257</b> |
| Romsey         | £134,804        | £175,882        | £192,172        | £205,898        | <b>£177,189</b> |
| Rural*         | No Details      | £165,000        | £198,333        | £297,790        | <b>£220,374</b> |
| <b>Average</b> | <b>£119,825</b> | <b>£158,661</b> | <b>£177,669</b> | <b>£227,422</b> | <b>£179,273</b> |

\*= Including Kings Sombourne / Middle Wallop / Broughton / Nether Wallop / Chilbolton

**Graph 2: Total Number of Each Unit Type for Sale as of 26th March 2004**



**Graph 3: Total Number of Units**



**Table 2: Total Number of Each Unit Type for Sale as of 9th September 2004**

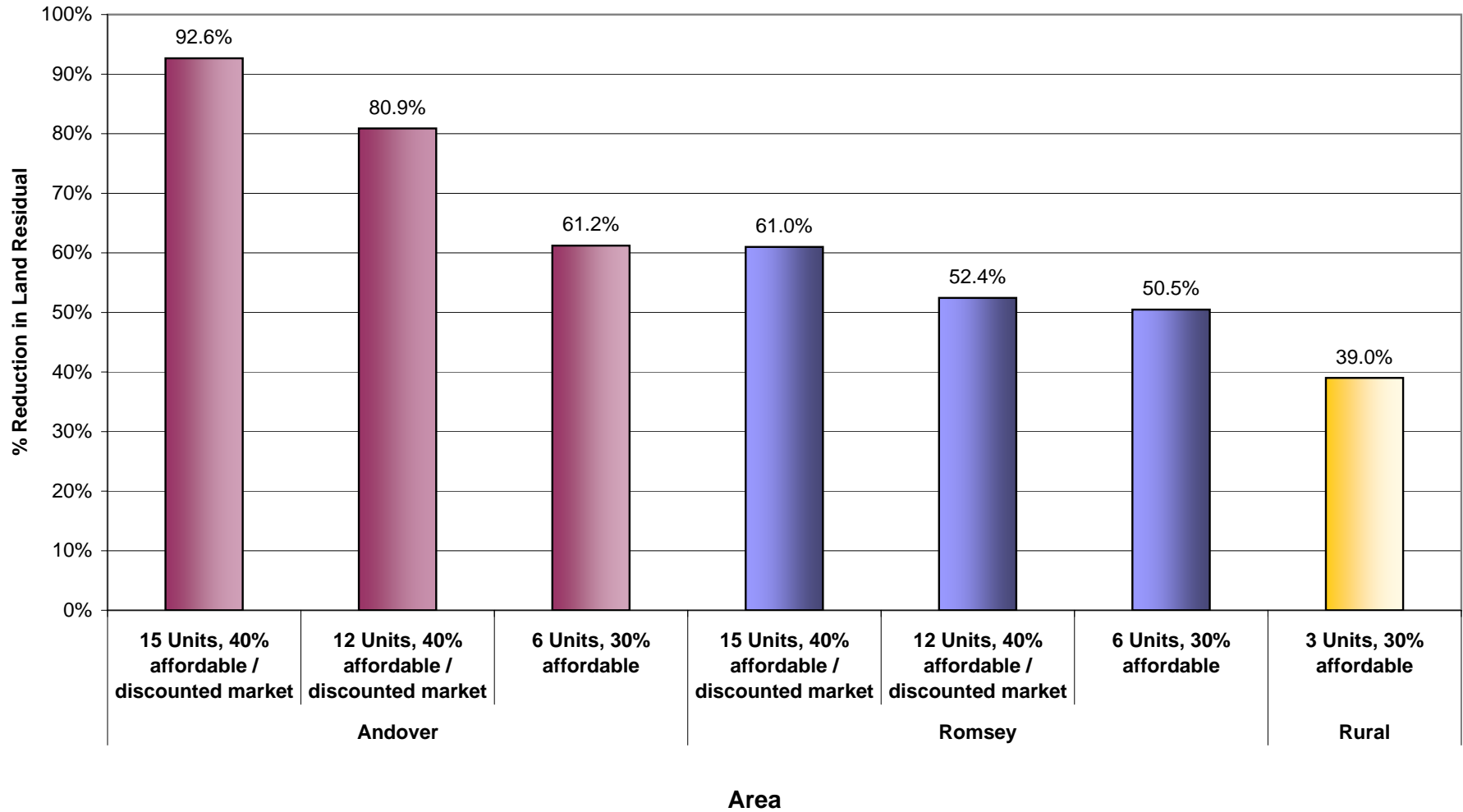
| Area               | Dwelling Type |            |             |             |
|--------------------|---------------|------------|-------------|-------------|
|                    | 1 Bed Flat    | 2 Bed Flat | 2 Bed House | 3 Bed House |
| Andover            | 12            | 36         | 29          | 137         |
| Romsey             | 9             | 11         | 18          | 58          |
| Rural*             | No Details    | 1          | 3           | 10          |
| <b>Total</b>       | <b>21</b>     | <b>48</b>  | <b>50</b>   | <b>205</b>  |
| <b>Total Units</b> | <b>324</b>    |            |             |             |

\*= Including Kings Sombourne / Middle Wallop / Broughton / Nether Wallop / Chilbolton

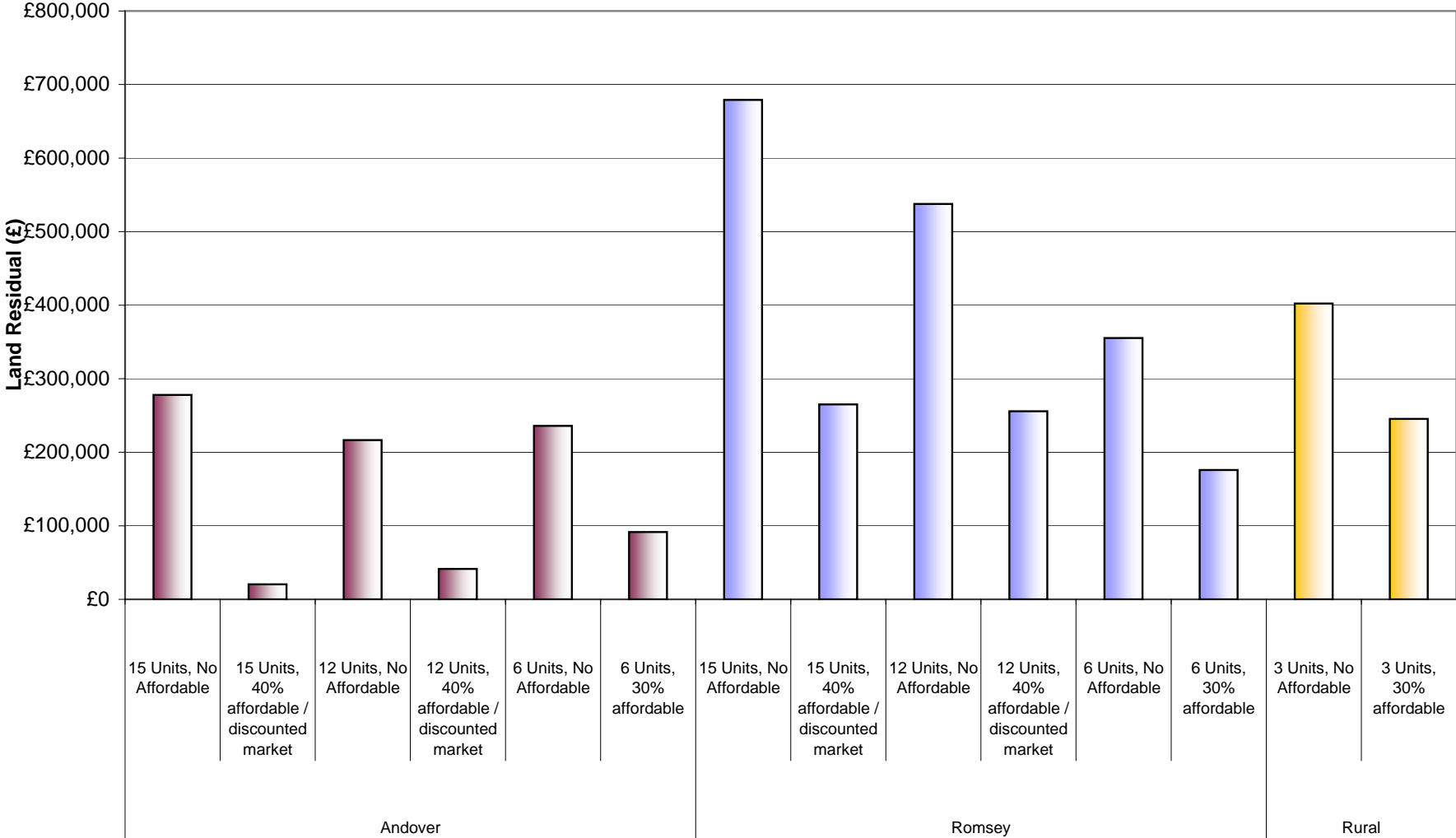
**Table 3: Summary Table Showing Reduction in Land Residual Based on Transfer of Affordable Units at in Return for Reasonable Build Costs**

| 1        | 2  | 3          | 4                | 5                       | 6                    | 7                   | 8                        | 9   |
|----------|--|------------|------------------|-------------------------|----------------------|---------------------|--------------------------|---|
| Location | Unit Mix                                     | GDV        | Development Cost | Developer Profit (@15%) | Finance & Land Costs | Residual Land Price | % Land Residual (of GDV) | % Reduction in Land Residual (From Zero Affordable Housing) |
| Andover  | 15 Units, No Affordable                      | £1,875,235 | £1,113,566       | £281,285                | £202,444             | £277,940            | 14.8%                    | N/A   |
|          | 15 Units, 40% affordable / discounted market | £1,505,741 | £1,102,315       | £225,861                | £157,132             | £20,433             | 1.4%                     | 92.6%   |
|          | 12 Units, No Affordable                      | £1,500,188 | £890,853         | £225,028                | £167,775             | £216,532            | 14.4%                    | N/A   |
|          | 12 Units, 40% affordable / discounted market | £1,247,440 | £883,201         | £187,116                | £135,741             | £41,383             | 3.3%                     | 80.9%   |
|          | 6 Units, No Affordable                       | £1,071,456 | £562,072         | £160,718                | £112,742             | £235,923            | 22.0%                    | N/A   |
|          | 6 Units, 30% affordable                      | £874,304   | £556,715         | £131,146                | £94,931              | £91,513             | 10.5%                    | 61.2%   |
| Romsey   | 15 Units, No Affordable                      | £2,432,860 | £1,121,930       | £364,929                | £266,834             | £679,166            | 27.9%                    | N/A   |
|          | 15 Units, 40% affordable / discounted market | £1,840,316 | £1,107,333       | £276,047                | £191,934             | £265,001            | 14.4%                    | 61.0%   |
|          | 12 Units, No Affordable                      | £1,946,288 | £897,544         | £291,943                | £219,228             | £537,573            | 27.6%                    | N/A   |
|          | 12 Units, 40% affordable / discounted market | £1,541,234 | £887,608         | £231,185                | £166,774             | £255,667            | 16.6%                    | 52.4%   |
|          | 6 Units, No Affordable                       | £1,235,388 | £564,531         | £185,308                | £130,312             | £355,237            | 28.8%                    | N/A   |
|          | 6 Units, 30% affordable                      | £983,592   | £558,354         | £147,539                | £101,761             | £175,938            | 17.9%                    | 50.5%   |
| Rural    | 3 Units, No Affordable                       | £893,370   | £286,401         | £134,006                | £70,703              | £402,261            | 45.0%                    | N/A   |
|          | 3 Units, 30% affordable                      | £675,580   | £281,934         | £101,337                | £46,986              | £245,323            | 36.3%                    | 39.0%   |

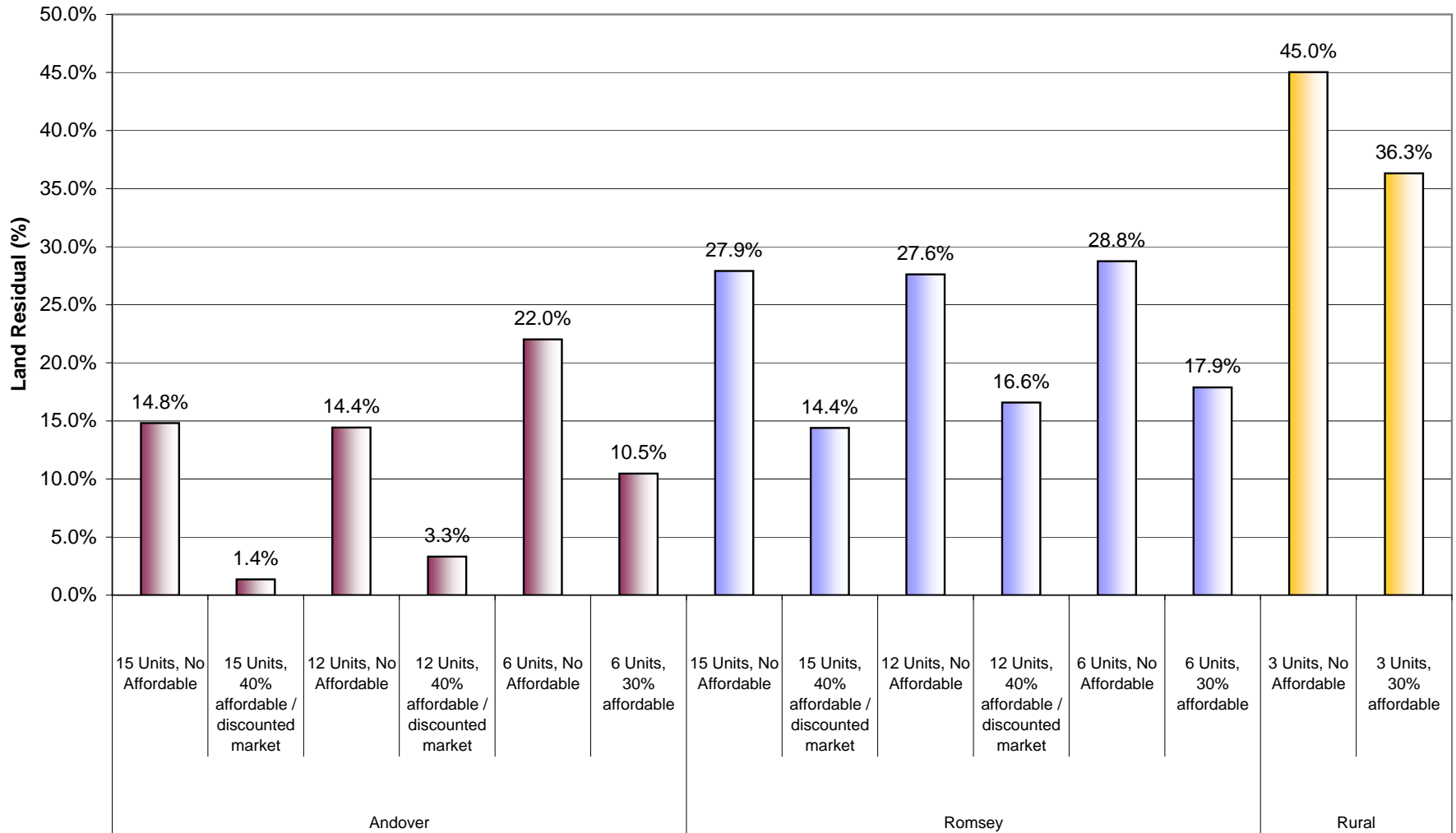
**Graph 4 Showing % Reduction in Land Residual Value in the 3 Model Areas from Zero to 40% Affordable Housing on 15, 12 and 6 Unit Schemes in Urban Areas and 3 and 2 Units in Rural Areas**



**Graph 5 Showing Approximate Residual Land Values**



**Graph 6 Showing Approximate Residual Land Value as Percentage of GDV**

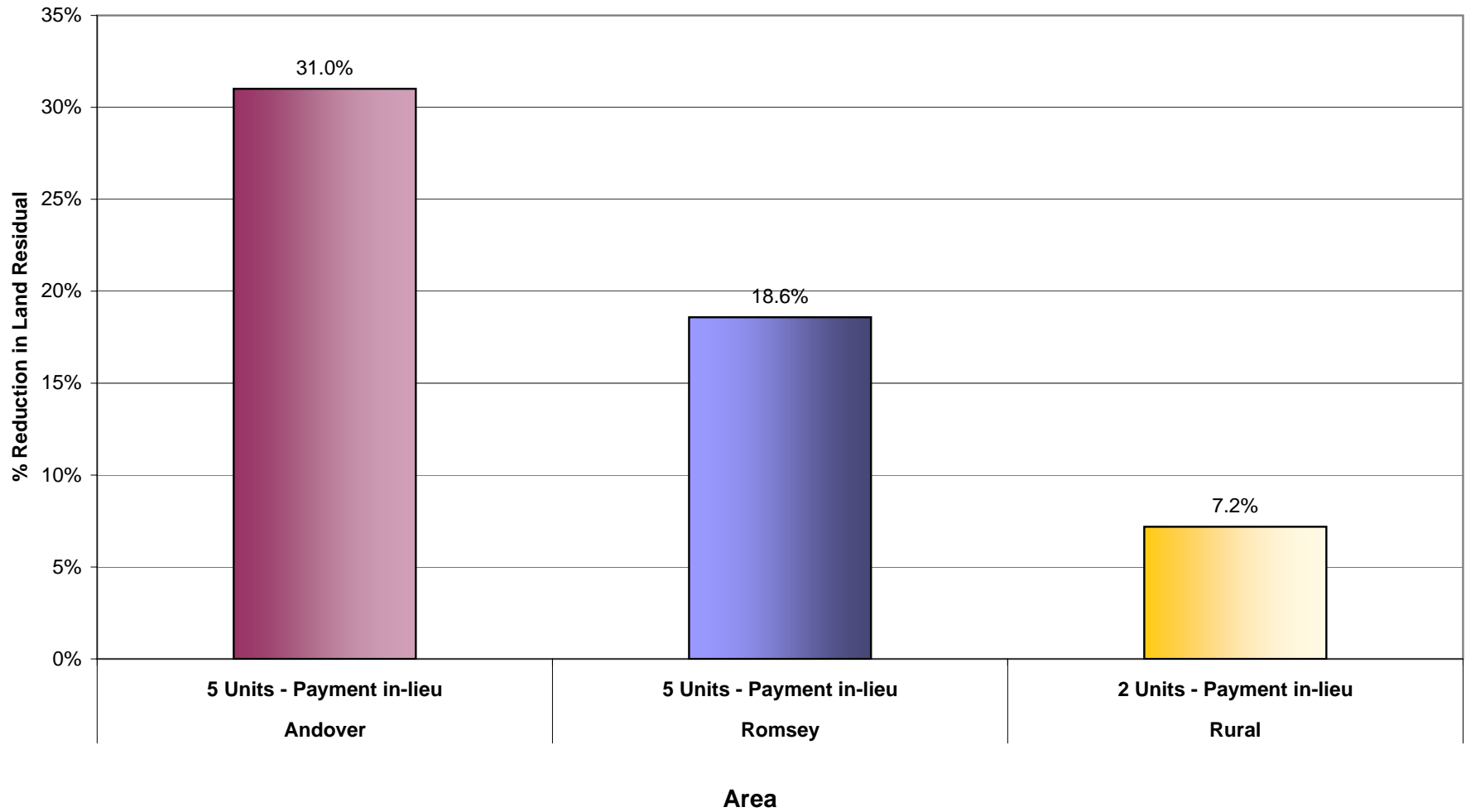




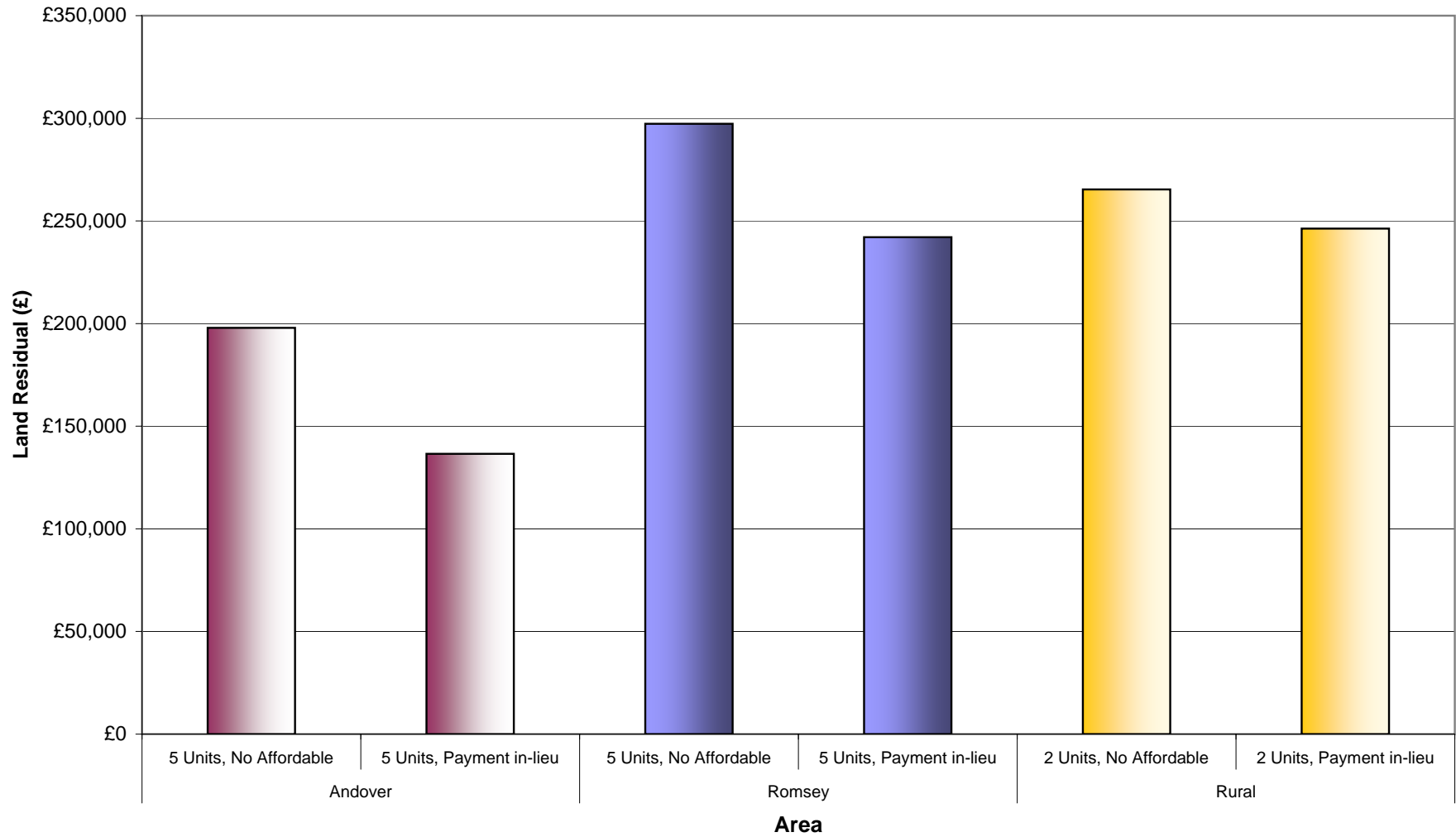
**Table 4: Summary Table Showing the Reduction in Land Residual Based on Commuted Payments in-lieu of On-Site Provision in Each of the Model Areas**

| 1        | 2                        | 3          | 4                | 5                       | 6                    | 7                   | 8                        | 9   |
|----------|--------------------------|------------|------------------|-------------------------|----------------------|---------------------|--------------------------|---|
| Location | Unit Mix                 | GDV        | Development Cost | Developer Profit (@15%) | Finance & Land Costs | Residual Land Price | % Land Residual (of GDV) | % Reduction in Land Residual (From Zero Affordable Housing) |
| Andover  | 5 Units, No Affordable   | £892,880   | £468,393         | £133,932                | £92,656              | £197,898            | 22.2%                    | N/A   |
|          | 5 Units, Payment in-lieu | £814,880   | £468,393         | £122,232                | £87,727              | £136,528            | 16.8%                    | 31.0%   |
| Romsey   | 5 Units, No Affordable   | £1,029,490 | £470,442         | £154,424                | £107,324             | £297,300            | 28.9%                    | N/A   |
|          | 5 Units, Payment in-lieu | £951,490   | £470,442         | £142,724                | £96,265              | £242,059            | 25.4%                    | 18.6%   |
| Rural    | 2 Units, No Affordable   | £595,580   | £190,934         | £89,337                 | £49,953              | £265,357            | 44.6%                    | N/A   |
|          | 2 Units, Payment in-lieu | £564,380   | £190,934         | £84,657                 | £42,510              | £246,280            | 43.6%                    | 7.2%  |

**Graph 7 Showing % Reduction in Land Residual Value in the 3 Model Areas when Commuted Payments are Received in-lieu of On-Site Provision for 5 Units in the Urban Areas and 2 Units in the Rural Areas**



**Graph 8 Showing Approximate Residual Land Values (Commuted Payments in-lieu of Affordable Housing Below the Thresholds)**



**Graph 9 Showing Approximate Residual Land Value as Percentage of GDV (Commuted Payments in-lieu of Affordable Housing Below the Thresholds)**

