Final Review of the Viability Report on the Development of WING

On behalf of South Cambridgeshire District Council

December 2015
Rev B

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Preamble and Background

In the first instance, it may be helpful to clarify that a Viability Appraisal can be carried out as a Residual Land Value (RLV), or as an appraisal to deduce the profit to be made on the basis that the land is a fixed cost. Essentially, an RLV deducts from the total income (GDV), the expected construction/development costs, planning obligations, plus an amount for developer's profit, so as to derive the site value. This value is compared to a "Benchmark Land Value" which is the value at which the land should be released by the land owner for development. If this value cannot be achieved then the scheme is unlikely to be brought forward.

In contrast, the alternative appraisal deducts from the total income (GDV), the expected construction costs, finance, marketing and a fixed amount for the Land Value, so as to derive the developer's profit. If this profit is at or above an acceptable level, the scheme will be viable but, if there insufficient profit, it will not be viable. In that event, adjustments would need to be made, for example by changing the market/affordable housing mix, so as to increase the GDV, or by reducing the Section 106 financial contributions, assuming all other costs are fixed.

Site value as a benchmark is defined in the RICS Guidance Note 'Financial viability and planning' (GN94/2012) as:

> *'Site value should equate to the market value, subject to the following assumption: that the value has regard to development plan policies and all other material planning considerations and disregards that which contrary to the development plan.'*

This will be influenced by its Existing Use Value (EUV) or an Alternative Use Value (AUV). In the case of the subject site, the EUV comprises retail car sales, workshops and open spaces. Market Value should also take account of the value of the site in the expectation that a (compliant) planning permission may be granted for residential development.

The point is that the land owners would not sell the land for less than it is worth. Indeed, the National Planning Policy Framework (NPPF) states that viability should consider competitive returns to a willing land owner and willing developer, to enable the development to be deliverable.

In paragraph 173 of the NPPF, it states:

> *'... To ensure viability, the costs of any requirements likely to be applied to development, such as requirements for affordable housing, standards, infrastructure contributions or other requirements, should, when taking into account the normal cost of development and mitigation, provide competitive returns to a willing land owner and a willing developer, to enable the development to be deliverable.'*

In this case, the Market Value of the site is agreed between the consultants at [redacted] and this is the benchmark value against which the Residual Land Value derived from an appraisal of the scheme is compared.

However, of particular importance to this scheme, as it is a Planning Policy document, is the Area Action Plan which states:

> *'The appropriate level of contribution sought from the development will take into account costs which fall to the development, including relocation of the airport and associated activities and elements of the North Works site.'*

So the costs of relocation are a scheme cost which must be allowed for in carrying out the financial appraisal to deduce the Residual Land Value. These have been estimated at [redacted] and have been the subject of extensive interrogation by a firm of independent quantity surveyors acting for the Council. The overall cost has been reduced and now deemed reasonable.

Following a joint submission by the Councils and the applicant, Counsel Simon Bird QC opined that, subject to the Council being satisfied as to their reasonableness, relocation costs are allowable and that these costs could include for replacement land value for the relocated businesses. The effect of this is to render the development unviable with 40% affordable.

The Councils' consultants queried the concept of this, particularly on the point that Marshalls would then be receiving new replacement buildings in the place of their existing older ones, without the appraisal taking into account this 'betterment'.

Marshalls sought their own Counsel's Opinion on this matter from David Forsdick QC, who stated that there is no indication in the words used [in the AAP] that the costs falling to the development are anything other than the full costs of relocation.

We would, therefore, recommend if the Councils are still concerned on this point, that a second Counsel's Opinion be obtained on their behalf, to confirm that this is the correct interpretation of the AAP in the context of viability, (rather than in the context of compensation as Mr Forsdick had considered). In the event that the second opinion agrees with Mr Forsdick, Marshalls' offer with regard to S.106 obligations and affordable housing is considered to be reasonable, as detailed in the final review that follows.

1.0 Executive Summary

1.1 Bespoke Property Consultants (BPC) and Carter Jonas (CJ) have been instructed by South Cambridgeshire District Council to review the viability report and appraisal submitted by the applicants Marshal Group Properties Ltd.

1.2 We have been involved with the scheme since late 2014 and have been provided with appraisals in the intervening period which have followed the scheme proposals' evolution and our comments on them.

1.3 We issued our initial report in April 2015 and this was followed up by detailed cost analysis by consulting quantity surveyors Silver DCC in August and September 2015.

1.4 We issued our penultimate report by letter on 14 October 2015 (Appendix B).

1.5 By even date the applicant issued a 'without prejudice' offer in respect of the affordable housing offer for the scheme. This offer proposes 30% affordable housing with 70% intermediate tenure and 30% affordable rented tenure. It also proposes a cascade mechanism to change the tenure split if intermediate shared ownership units cannot be sold to an RP at the time of delivering each phase.

1.6 The applicant has followed up the offer with a letter dated 26 November 2015 (Appendix A) giving commentary on our letter of 14 October 2015 and enclosing opinion from Counsel on the issue of the value of the relocated premises.

1.7 We set out below in section 2 of this report our comments on the applicant's letter and in section 3 our comments on their latest scheme appraisal.

1.8 We would draw the Council's attention to the need to secure the matters set out in the paragraphs below which relate to

a) Lifetime Homes Standards

b) Joint and several liabilities of the landowner and developers

c) Ensuring the cascade mechanism operates in a sequential manner and not in the alternative manner proposed.

d) Ensuring the cascade mechanism can increase as well as decrease the overall number of affordable units depending on the value achievable for those units.

e) Ensuring that in assessing the value of the affordable units a thorough tendering process to RPs and other providers is adopted.

f) Securing the delivery of the scheme on a phase by phase basis, with 50 units taken to slab level within two years of detailed planning consent being granted.

1.9 An issue which has been at the centre of our discussions on viability with the applicant concerns the impact of relocation costs. The Area Action Plan states that relocation costs (which add up to about [redacted] can be taken into account. Without this as an extra, the scheme would be viable with policy compliant affordable housing. It is the obligation to include this as an extra cost which tips the balance on viability.

Linked with this is the concept of how the value created in the relocated buildings could be used to off-set the cost of relocation of these buildings.

The applicant has sought independent advice from Counsel in this regard who has opined that for viability purposes full relocation costs are allowable in addition to their existing value. We remain concerned on this issue and believe if the Council are also concerned then the matter should be referred to Mr Simon Bird QC who was jointly instructed by the Council and the applicant on the scope and relocation costs in January 2015.

That said we acknowledge that the AAP policy wording is silent on this issue and we doubt it was contemplated when the policy was drafted. It is also true to say, as advised by the applicant that there is an opportunity cost to the use of Marshalls' own land within the relocation scheme.

1.10 Turning to our conclusion on the financial viability we would advise as follows

It is our opinion that the provision of 30% affordable housing with a 70/30 tenure split (intermediate/affordable rented) with S.106 contributions of £28,234,269 is a viable offer.

We disagree with the applicant that this will reduce the residual land value by [redacted] below the benchmark land value, because the cumulative effect of the adjustments we have noted below bring the RLV within an acceptable tolerance of the benchmark:

	£
Residual land value per Arcadis appraisal	[redacted]
Ground rent income increase	[redacted]
Non-residential income increase	[redacted]
Site wide infrastructure saving	[redacted]
Relocation cost saving	[redacted]
Engine running bay saving	[redacted]
Reduced fees on cost savings (10%)	[redacted]
Reduced DM fee on cost savings (1.5%)	[redacted]
	[redacted]
Benchmark land value	[redacted]
Final difference	**£1,607,455**

1.11 For the above reasons if the advice we have given in respect of the drafting and content of the S.106 Agreement is adhered to, we believe the overall offer as set out by the applicant on 14 October 2015 is reasonable and viable to be delivered bearing in mind the AAP policies.

2.0 Marshalls' letter dated 26 November 2015

We would comment on the points raised in this letter and the attached offer as follows:

2.1 **Perceived 'betterment'** As set out in our letter dated 14 October 2015, we have advised the Council that if full relocation costs (ie replacement of existing buildings) and the market value of the site are allowed within the appraisal, then the applicant will benefit from the increased value of new premises provided as a development cost over the old premises being replaced, as well as the residual land value of the proposed scheme.

Marshalls' position is that they believe the policy wording in the AAP allows them to recover the relocation costs in full, without regard to the value of the new premises. Further they have sought Counsel's opinion to support this argument. Counsel focuses on the use of the term 'betterment' by us, which in hindsight may not have been entirely appropriate, as it has connotations of statutory compensation and CPOs. This was not our intent, as we merely wished to point out that the applicant will benefit from both the relocation / rebuilding of their premises as well as the land value attributed to the development.

We do not dispute that the scheme needs the present businesses to be relocated in order to proceed, but we do not agree with Counsel's view that the applicant will not seek to realise the improved value of their assets at some stage, either by sale or mortgage.

That said, taking into account the policy direction of the NPPF to encourage rather than constrain development, and in particular that a land owner should get a return on the land value, we conclude this is very much a matter of negotiation. The AAP policy wording is silent on the issue of value and we do not think it was drafted in contemplation of the issue we have raised. Therefore the acceptance, or not of the position put forward by the applicant needs to be judged in light of the overall S.106 package offered by the applicant and its mitigation of the effects of development as required by CIL Regulation 122. If the Council remains concerned on this point, it can refer the matter to Mr Simon Bird QC, who gave the original opinion instructed by both parties in January 2015.

2.2 **Review Mechanisms** As set out in our letter dated 14 October 2015, when a non-policy compliant offer is made on a large scheme such as WING it is standard practice to include a viability review mechanism to see if the scheme can offer additional S.106 benefits at a future

date. This is particularly relevant in the case of affordable housing as in most cases it is the element of a S.106 package which gets reduced to allow for other generally financial and infrastructure based items to be provided. Clearly the latter mitigate the impact of development as required by CIL Regulation 122.

It is also clear from the NPPG that S.106 obligations should not be an impediment to development being brought forward. It is therefore balancing the need to encourage / expedite development and securing the maximum reasonable amount of S.106 obligations that must be achieved.

In this case the applicant contends that review mechanisms set against individual phases (which we suggested should comprise 200 units each) would not be a workable solution, as most of the relocation costs take place in the final phases of the scheme.

We understand this issue, and as such it raises a further concern that the early phases may easily be delivered, with a lower affordable housing offer than policy requires, and then the applicant may seek to revisit the affordable housing delivery in the final phases due to unforeseen or increased costs in relocating the businesses on the North Works. There is no overall solution to this risk at this stage, but the Council needs to be aware of it and make the drafting of the S.106 as secure as possible to ensure delivery of the affordable housing across the site.

The applicant has stated the omission of a review mechanism will give it and the eventual developer of the site more certainty which will allow the scheme to be brought forward quicker. We concur with this view and agree that it will help in this regard as developers and their funders prefer not to have to deal with such mechanisms.

The effect of that is, it should be easier for the applicant to agree delivery timescales and we note that they have made a proposal in their offer of 14 October 2015 to deliver 50 units to slab level within two years of full planning approval being granted for the first phase (including reserved matters approvals). This is an important commitment as it would necessarily mean the construction of significant infrastructure which will benefit the whole scheme. Such commitments to delivery are encouraged by government policy and could also be used on subsequent phases.

If the construction of 50 units to slab level is not achieved in the specified timescale, then a fresh viability assessment of the whole scheme should be triggered. As such we are satisfied that this sort of delivery mechanism with the fallback position of a further viability review is appropriate in these circumstances with the stated aim of expediting delivery of the scheme, and similar provisions should be considered for subsequent phases.

2.3 **S.106 costs** – we note that Marshalls' letter of 26 November 2015 states that S.106 costs are 'largely agreed'. This is supported by your instructions to us and we are working on the basis that the total sum of £28,234,269 in the Arcadis Appraisal as shown at Appendix B (attached) is correct.

We note the applicant states that due to the amended triggers for payments a saving of [redacted] has been achieved, and their offer is contingent on these triggers being accepted. If they are accepted they will have to be included in a clear and concise manner in the S.106 in the interest of both parties.

2.4 **Affordable Housing delivery** – Marshalls' letter of 26 November 2015 sets out the well-known issues that have begun to negatively influence the delivery of affordable rented housing. We agree with this, and the fact that government policy is now firmly aimed at encouraging home ownership and forms of tenure that lead to that end.

As yet we and indeed the applicant are unaware of the details of the secondary legislation that will enact the changes proposed in the Housing and Planning Bill including the introduction of 'Starter Homes'. What is clear is that if implemented in the fashion that ministers have suggested, then Starter Homes will be beneficial to the viability of a scheme as they will derive an increased value for this type of unit over that for rent or shared ownership properties. We would therefore advise that to ensure consistency, if the proposed offer of 70% shared ownership units and 30% affordable rented units is accepted, then the S.106 Agreement should preclude the transfer of these units to Starter Homes, without a commensurate increase in the number of units provided by the increase in value created. This is a simple mechanism to include in the S.106 Agreement as the percentage of open market value for the shared ownership units is set at 66.45% in the Arcadis appraisal. The anticipated value of Starter Homes is likely to be 80% so an increase of 20% in the number of units provided can be calculated as fair and reasonable for such a tenure change.

The above proposal can be factored into the detailed drafting of the S.106 Agreement, dealing with the first stage of the cascade mechanism proposed by the applicant. Such drafting would and should allow the flexibility the applicant is seeking, in addressing the market for affordable housing at the appropriate time. The applicant is right to point out this is needed to ensure continuity in the development and avoid the S.106 constraining delivery.

The applicant advises that the triggers in the cascade mechanism is there to explore alternative tenure solutions should there be a shortage of demand for shared ownership properties. This we believe is a concern shared by your housing officers.

We would advise that to keep the cascade simple and to avoid the need for a full viability review within the cascade mechanism, that the judgement as to whether 'the modelled scenario cannot be delivered in any given phase' is limited to the value of the affordable housing as set out in the Arcadis appraisal not being achieved. The value per phase of the affordable housing can be pro-rated from the figures provided by Arcadis. This is broadly consistent with the cascade terms set out by the applicants' solicitors.

It would be sensible to have a fixed minimum for the level of affordable housing such that all parties understand the approach that is being taken and the parameters they are working within when looking at different tenure mixes.

Clearly the final stages of the cascade leading to the Council buying affordable units or the applicant making a payment in lieu should only be considered when the other stages have failed and not as an alternative as suggested by the applicant. For the previous stages to have failed it is more likely that the market will have collapsed and the whole scheme would be stalled leading to further negotiation / amendment of the S.106 in any event.

2.5 **Final Position** The letter from Marshalls summarises the offer dated 14 October 2015 as the provision of 390 affordable homes with a tenure split of 70/30% between intermediate and affordable rented housing. It is stated to be on the basis of the 'principles... we have set out above', which we assume to mean the delivery mechanism for the scheme, the S.106 payments totalling £28,234,269, with consequent triggers for payment and the affordable housing cascade mechanism.

The applicant concludes that the offer results in a deficit of [redacted] comparing the residual land value to the benchmark land value they have adopted for the site. This deficit is calculated by the Arcadis appraisal which we discuss in detail in section 3 below.

3.0 Arcadis (EC Harris) Appraisal V005(48) WING

We have reported on the appraisals for the scheme as they have evolved since late 2014, we will therefore not comment in detail here where matters have been agreed.

3.1 Sales Values

The latest appraisal shows an average sales value of £410.16/ft² with a total value of [redacted] for the 910 open market sale units. As per our letter of 14 October 2015, we remain of the opinion that this value is conservative when judged against the current market and the quality for the proposed scheme.

There have been recent changes in 'Buy to Let' market in terms of

a) Income tax changes (July 15 Budget)

b) SDLT increase of 3% (Nov 15 Autumn Statement)

c) Mortgage restrictions (now applied in anticipation of BoE regulation).

In view of the very strong BTL market in Cambridge, particularly from private investors, this may have an impact on pricing within a few months, especially in April 2016 when the SDLT changes are implemented.

However, this should be balanced against many of the current house price forecasts for Cambridge which predict further price increases in the foreseeable future.

3.2 Unit Sizes

Despite the comments in the applicant's response of 14 October 2015 (annex 2 to the 26 November 2015 letter) we remain of the opinion that the 3-5 bed units are large in terms of net internal area and therefore could be reduced by a future developer to make the scheme more viable. This factor also contributes to reducing the average price per ft² as noted in 3.1 above. The aspiration to achieve Lifetime Homes for all units should be set out in the S.106 Agreement to ensure delivery of the required standard and hence net internal areas.

3.3 Ground Rents

In our letter of 14 October 2015 we put forward advice that ground rents should now be in the range of [redacted] per annum and not [redacted] as stated by the applicant. This follows research by Carter Jonas into ground rents being charged on local developments which now include more frequent rent reviews often index-linked. Recent ground rent sales in Cambridge suggest

that an additional £275,000 could be achievable based on the total ground rent income or up to £500,000 if a modern review clause is also incorporated.

3.4 **Affordable Rented Income**

TAs with our comments in our letter of 14 October 2015, we remain of the opinion that the values used are low, and lacking in justification. It is usual to obtain indicative offers from a range of registered providers even at this early stage, as RPs will be interested in engaging with scheme promoters to secure a position going forward. However in terms of the cascade mechanism put forward and our comments above about changes in tenure, having a lower affordable housing value will make it easier to maintain or increase the overall number of affordable units if tenures with higher values are used, but this would be at the cost of reducing the number of rental units.

3.5 **Non-Residential Income**

The applicant has provided further commentary as to the valuation of the petrol filling station, with which we are now satisfied on the basis of the omission of its construction cost as the applicant has stated.

We would note that the current appraisal has an error in it, in reference to the value of the coffee shop. No yield or purchaser costs have been applied so the appraisal has the capital value of the shop equating to one year's rent. If a yield of 6% is applied (assuming a branded chain is the occupant) then the value would increase by [redacted].

3.6 **Developer's Margin**

The applicant has responded on the point raised in our letter of 14 October 2015 and we are now satisfied with the margins applied to each element of the scheme. We still believe the margins applied are at the low end of the spectrum for a large scheme such as this.

3.7 **Build Cost**

We are satisfied that in the period this scheme has been under review the base build costs and external works have now risen sufficiently to justify the applicant's suggested figure of £137/ft^2 for these works.

3.8 **Basement Parking**

We note that the scheme design requires the inclusion of 150 basement parking spaces and in reviewing the scheme applied for we must advise the Council of the negative effect this has on the viability of the scheme being at a cost of £4.8M.

In the end the inclusion of such a requirement is a matter for planning policy and design judgement. As the scheme is not fully designed, we can understand why Arcadis have used a relatively high value per space at £32,000. Whether this figure is eventually accurate will depend on the efficiency of the design and the ground conditions encountered. We can confirm it is within the normal range of such costs but as previously stated, at the upper end.

3.9 **Development Management Fee**

We are satisfied with the explanation provided by the applicant in respect of the level of the fee. We would advise the Council, based on experience of other large schemes, that provision of an overarching development manager is essential in coordinating the infrastructure provision and the developers of each phase.

The Council will need to consider in the drafting of the S.106 the joint and several liabilities of the land owner and future developers of the individual phases. Having a development manager to coordinate and report on S.106 triggers will assist this, but the reporting must also be clearly set out in the S.106 agreement.

3.10 **Site wide infrastructure**

As you are aware, these costs were fully reviewed by Silver DCC in August 2015. Of the [redacted] of savings Silver identified, only [redacted] has been accepted by Arcadis. Arcadis have also indexed the costs upwards by [redacted] and we believe there may be some overlapping of timescales in this respect. Overall the applicant states that the infrastructure costs have been reduced by [redacted] since the cost plan reviewed by Silvers. It is our opinion, based on the advice of Silver DCC, that the infrastructure costs are overstated by up to [redacted] whilst allowing for indexation since 2015.

3.11 **Relocation costs**

We acknowledge that Silver DCC and the applicant are very close in terms of the overall relocation and rebuilding costs. The difference of [redacted] in the total costs however remains

unexplained. With regard to the Engine Running Bay, Silver identified a cost difference of [redacted] and notwithstanding the response from the applicant on 22 September 2015, we remain of the opinion that this difference is still relevant.

We note and agree the comments of the applicant's solicitor in their instructions to Counsel that some of the Marshalls' businesses are to be relocated to Marshalls' own land and that there is as yet an undefined 'opportunity cost' for the use of that land in this regard.

3.12 **Funding costs**

We are in agreement with the applicant that the overall funding costs are reasonable.

3.13 **S.106 Costs**

We understand from Marshalls' letter that the S.106 costs have been agreed at £28,234,269. This cost is inclusive of Newmarket Road Corridor works and cycle bridge and Marshalls' letter confirms this. The triggers for payment will be as set out in Annex B of Marshalls' letter, and the S.106 Agreement will need to secure these.

3.14 **Conclusion on Appraisal Inputs**

Taking account of the points made above, it is our opinion that the provision of 30% affordable housing with a 70/30 tenure split (intermediate/affordable rented) with S.106 contributions of £28,234,269 is a viable offer.

We disagree with the applicant that this will reduce the residual land value by [redacted] below the benchmark land value because the cumulative effect of the adjustments we have noted bring the RLV within an acceptable tolerance of the benchmark as noted below:

	£
Residual land value per Arcadis appraisal	[redacted]
Ground rent income increase	[redacted]
Non-residential income increase	[redacted]
Site wide infrastructure saving	[redacted]
Relocation cost saving	[redacted]
Engine running bay saving	[redacted]
Reduced fees on cost savings (10%)	[redacted]
Reduced DM fee on cost savings (1.5%)	[redacted]
	[redacted]
Benchmark land value	[redacted]
Final difference	**£1,607,455**

Appendix A

MARSHALL GROUP

PROPERTIES LTD

THE AIRPORT, CAMBRIDGE, CB5 8RX

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26th November 2015

Mr P Mumford
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WITHOUT PREJUDICE

Dear Paul

Wing – Viability Review
Response to Carter Jonas Letter dated 14th October 2015

Further to recent discussions with regards the viability model and S106 Heads of Terms, I write to address the points raised in the Carter Jonas letter dated 14th October 2015. This was written in response to the Marshall submission dated 22nd September (and the accompanying report and financial model by ARCADIS).

Given Carter Jonas's written response crossed over with Marshall's Without Prejudice offer (also dated 14th October 2015), the comments in the letter do not take into account Marshall's proposed revised position. Annex 1 to this letter includes the offer in full for reference.

For the sake of completeness and transparency, I address each of the points raised by the Carter Jonas letter in turn, taking into account of our Without Prejudice position, whereby Marshall has offered to accept a reduction in the residual land value of [redacted].

I address in the main body of the letter the key points of principle, with the other matters raised in the letter being picked up in Annex 2 to this letter.

1. **Points of principle**

1.1 Perceived 'betterment'

Background

The letter raises again the concept of perceived 'betterment' to the landowner as a result of relocating existing businesses to new facilities and suggests that additional value is realised.

The advice of Simon Bird QC (jointly instructed by the parties in January 2015) is unequivocal when it comes to interpretation of CEAAP (2008) policy CE/33 which states "the appropriate level of contributions sought from the development will take into account costs which fall to the development, including relocation of the airport and associated activities and elements of the North Works." (my emphasis).

His advice was that it is the full cost of business relocations required to deliver the scheme that should be reflected in the viability appraisal. An extract from paragraph 5 is included below:

> *"5. In terms of the allowable costs in relation to relocation, those must reflect all the costs which the business needs to receive in order to facilitate the extent of relocation which the wider design process has shown to be appropriate. Such costs properly include the land/premises costs, construction costs of new buildings and potentially removal costs. However, costs which would have been incurred at some stage in the ordinary run of business, irrespective of the development are not sensibly allowable. " (my emphasis)*

He goes on to say at paragraph 6:

> *"6. As to the relocation costs utilised by E C Harris in their draft appraisal, it will clearly be necessary for the Council to be satisfied as to their reasonableness."*

Reasonable Relocation Costs

On the latter point, the Council have now sought advice on all aspects of the viability appraisal and the costs have been interrogated by the Councils' advisers, including Cost Consultants Silver DCC. The abnormal costs have (in large part) been agreed, albeit Marshall acknowledges there are some small residual differences between the parties, which are relatively small in the context of the scheme overall.

The Council's advisers position

The Council's advisers continue to argue that there is a case to be made that Marshall is unduly benefitting from the value created from relocating businesses from existing buildings to purpose built new premises, a concept that has been described as 'betterment'. This was not specifically mentioned in Simon Bird QC's advice which pre-dates this point being raised by the Council's advisers.

Our position on this is set out on page 15 of our 22nd September 2015 response as follows:

"Betterment
Marshall and Arcadis have reviewed the comments made in the Carter Jonas report regarding the concept of 'betterment' (paragraphs 2.1, 2.3 (c), 4.5.4.2 (a) and 5.3 refer). In light of this, Marshall have sought advice from Mills & Reeve's on precedent cases for reflecting so called betterment in planning viability. Marshall have also engaged with Bidwells to understand whether there is a recognised approach to addressing this comment.

The advice received is resounding in that there are no relevant precedents for accounting for this in planning viability and as such our submission takes no account of so called betterment."

Marshall has asked Council officers on more than one occasion to seek guidance from their advisers on any precedent cases, or a proposed methodology for addressing this matter. To date, no guidance has been given and no precedent cases identified. The point was again raised in a meeting with officers on 7th October 2015, and subsequently in the Carter Jonas letter dated 14th October 2015.

With the objective of concluding matters, Marshall sought an objective opinion from David Forsdick QC, and both the instructions and opinion have been shared openly with Council officers (see appendix A of our 'Without Prejudice' offer dated 14th October 2015). This was instructed by Marshall directly as the advice from Mills & Reeve was unambiguous and our objective was to reach a definitive position on the matter as promptly as possible.

David Forsdick QC's advice (dated 13th October 2015) states at paragraph 1, the following:
"given the interpretation of the applicable policy and the relevant valuation framework, I do not think that the concept of "betterment" is relevant in this context". At paragraph 9 he states *"in my view there is no indication in the words used [in the applicable policy] that the costs falling to the development are anything other than the full costs of relocation."*

Marshall considers the combined advice of Simon Bird QC and David Forsdick QC to be conclusive and supportive of the approach adopted by Marshall in our assessment of the scheme's viability.

1.2 Review mechanisms

In section 1.2 of the letter, Carter Jonas has invited the Councils to "consider a review mechanism" in the event a "non-compliant affordable housing offer is initially accepted", with a suggestion that no individual phase for review should be greater than 200 units.

In putting forward our without prejudice offer on 14th October 2015, Marshall were very clear that this was being made on the basis that there is to be **no periodic review of the scheme viability.**

Whilst Marshall believes the appraisal to be robust and a true reflection of the scheme's viability, we have offered to accept a shortfall in residual land value (i.e. the return to Marshall) of over [redacted]. We are therefore offering to take on considerable risk in the development process and we are not prepared to accept this position should a periodic or phased review mechanism be imposed. In addition, as highlighted in the review of the abnormal costs, a lack of project definition at this outline application stage means costs are uncertain, and in our view, on balance, are more likely to increase than reduce as the detailed proposals and designs emerge thereby increasing the risk apportioned to Marshall.

Marshall considers there to be considerable benefit in creating certainty in order that the scheme advances in a timely fashion, to ensure much needed housing is delivered, and to avoid undue complications securing a developer partner and in bringing forward subsequent phases of the development.

Under advice from Mills & Reeve, Marshall considers that the specific circumstances of the Wing development are not compatible with conventional approaches to viability review. We can understand how such a review may be appropriate where a scheme faces considerable up-front investment in infrastructure, as is normally the case for urban extensions, major urban regeneration projects or new settlements. In some circumstances, a reduced level of affordable housing may be accepted by local authorities in early phases to enable critical infrastructure to be delivered, with reviews on subsequent phases which are not encumbered with such significant infrastructure costs to allow increased delivery in later phases. We understand this to be the case at Northstowe where a reduced level of affordable housing (20%) has been agreed for the first phase, which carries a disproportionate burden in relation to infrastructure costs.

The Wing development is somewhat unusual due to the circumstances of the site. Save for the relocation of the engine running bay, which will be an early abnormal cost, the majority of the significant abnormal costs are incurred during the final phases of development which would make a periodic review, at say every 200 units, unworkable. The North Works phases comprise approximately 490 dwellings and these will be the final phases of development. Any periodic review prior to the 810th dwelling would not be able to take into account with any accuracy the abnormal costs on the final phases (North Works) – which would not have occurred and may not be accurately quantified at that time. In practice, the true costs of relocating the businesses would only be understood once they are completed.

Taking account all of the points above, Marshall is firmly of the view that a periodic or phased review mechanism is not appropriate in this case and that our 'Without Prejudice' offer represents the best outcome for the Councils given the circumstances of the scheme.

Marshall's Commitment to Delivery

Should officers be minded to accept the 'Without Prejudice' position presented by Marshall, we are willing to make a commitment to early delivery by entering into an obligation to undertake a full viability review in the event there are undue delays in bringing the scheme forward. In effect, a requirement on Marshall (and any development partner we may select) to bring the scheme forward promptly otherwise the viability position will be refreshed.

The nature of these obligations will need to be discussed and refined, but in principle we propose to offer to enter into an obligation for a full viability review in the event any of the milestone dates below are missed, leading ultimately towards completion of the first 50 dwellings to slab level within the prescribed timescales.

We would be willing to enter into the following obligations:

1) Within **nine months** of the grant of outline planning permission for Wing, as long as the permission has not been subject to legal challenge, an obligation to submit the planning application/EIA or permitted development consultation for the proposed Aircraft Ground Run Enclosure.

2) Within **18 months** of the grant of outline permission for Wing, as long as the permission has not been subject to legal challenge, an obligation to submit the following:
   a) The Design Code for approval;
   b) The first phase reserved matters application for approval;
   c) An application to discharge all pre-commencement planning conditions requiring details to be approved;

3) Upon full planning approval of 1) and 2) a, b and c above, and at such point as they are free from legal challenge, Marshall will from that point accept an obligation to ensure the foundations up to slab level for the first 50 dwellings are completed within **two years**.

In the event that these timescales are not met, Marshall would be supportive of a full rerun of the viability model. This would necessarily need to take account of all factors and market conditions which prevail at the time and would necessitate inputs and assumptions being updated.

Please note that these are proposed as long stop dates reflecting the risks associated with projects of this scale and the need to procure developers and/or contractors for all elements of the works.

Note - As officers are aware, detailed feasibility work is underway on relocating the Engine Running Bay to a purpose built Aircraft Ground Run Enclosure, which is a critical enabling project for Wing. Marshall is in the process of commencing a tendering stage to identify a potential supplier for the facility. The consenting route will need to be determined in due course.

3. S106 costs

3.1 Following further discussion between South Cambridgeshire District Council, Cambridge City Council and Cambridgeshire County Council, it is understood that the S106 Heads of Terms are now largely agreed, as incorporated in the viability model.

The only changes Marshall has proposed to improve viability, is the timing of the S106 triggers relating to the secondary school, Chisholm Trail cycle bridge and the contribution for improvements to Newmarket Road. The combined effect of adjusting the triggers, in accordance with Appendix B of our Without Prejudice offer, has been a [redacted] saving in financing costs.

The Without Prejudice offer put forward by Marshall is contingent on these triggers being accepted.

Flexibility in affordable housing delivery

There are currently a number of uncertainties in the market which are affecting the business plans of Registered Providers. The key challenges which have emerged in recent months are as follows:

- The Housing and Planning Bill and proposed introduction of Starter Homes. Although the 20% discount on market value, and proposed price cap of £250,000 is known, the implications for the affordable housing sector are unknown pending secondary legislation and guidance, assuming the Bill receives Royal Assent.
- Budget announcements in July 2015 imposed reductions in affordable rents from 2016 onwards – which have reduced scheme income from affordable housing;
- Implications of the proposed Right to Buy on social rented stock remains an unknown quantity.

Council Housing Officers have expressed particular concerns about the potential risk that there is insufficient demand for shared ownership properties, based on the household salary cap of £60,000 for qualifying households and the potential competition from Starter Homes as they come to the market. Based on our Without Prejudice proposal, the scheme would deliver 273 intermediate properties. The Chancellor's Autumn Statement (25 November 2015) sets out Government's commitment to increase the household salary threshold for shared ownership properties from £60,000 to £80,000 (outside of London). Marshall considers that this is likely to provide some comfort that there will be sufficient demand from qualifying households as this will bring a wider range of people into the qualifying criteria.

However, in the light of continuing uncertainty, Marshall believes some flexibility in the terms of the S106 are critical to ensure the scheme can be delivered as circumstances change over time – particularly as more clarity emerges in respect of the delivery of Starter Homes. It is also noted that Brandon Lewis in his letter to Chief Planning Officers of 9 November 2015 encourages flexible arrangements in s.106 agreements, to allow the delivery of alternative forms of affordable housing if this becomes necessary.

Marshall has engaged Mills & Reeve Solicitors to draft the key principles of a cascade mechanism with the objective of providing some flexibility in the approach to delivery. Annex 3 to this letter sets out proposed wording for inclusion in the S106 agreement, to be refined in discussion with officers as part of the detailed drafting of the S106.

This sets out Marshall's commitment that the starting position in any phase of the development will be delivery of 30% affordable housing, with a 30:70 tenure split in favour of intermediate housing, as set out in our Without Prejudice position. Given uncertainties in Government policies, and potential changing market conditions, some flexibility is proposed, which would only take effect by agreement of all parties.

The objective of the cascade is to take a staged approach to exploring alternative solutions in the event the modelled scenario cannot be delivered in any given phase. The key principles are:

- The first stage in the cascade would be to explore alternative forms of intermediate tenure, potentially to include Starter Homes or other intermediate tenures (e.g. Discount Market Value), should there be a shortage of demand for shared ownership properties.
- The second stage, if all first stage options have been exhausted, would be to review the tenure split to deliver more affordable rented properties, but with a proportionate adjustment to the headline percentage affordable in any given phase. For reference, looking at the scheme as a whole, based on a 50:50 tenure split, the headline percentage affordable to achieve the same residual land value would be 23%. If the Council is minded, Marshall would be willing to include 23% (50:50 tenure split) as a minimum level under the terms of the cascade.
- Two further stages are then included to provide options for the Council either to purchase the stock at an agreed price, or to accept a financial payment in lieu of on-site delivery as an absolute last resort.

Final position

In light of the above comments, Marshall considers the 'Without Prejudice' offer dated 14th October 2015 to be our final position on the viability of the scheme. By accepting the shortfall of [redacted] against the benchmark residual land value this shows a considerable commitment to bringing the scheme forward, with a headline rate of 30% affordable housing, with a 30:70 split between affordable rent and intermediate housing. This equates to a total of 390 affordable homes, of which 117 will be affordable rented and 273 will be intermediate.

As set out above, we are willing to commit to prompt delivery of the scheme in accordance with terms to be agreed with the Local Authority, the principles of which we have set out above.

We would welcome further advice from officers on how you wish to progress matters from here.

If you have any queries in the meantime, please do not hesitate to contact me.

Yours sincerely,

[redacted]

Richard Oakley
Development Director

Enc.

ARCADIS Financial Model – 30% affordable, 30:70 tenure split

ANNEX 1 - Without Prejudice Position 14th October 2015

WITHOUT PREJUDICE
14th October 2015

This note sets out Marshall's revised position on the viability of the Wing scheme, in the light of further discussions with officers of South Cambridgeshire District Council.

Background

Our latest submitted position was set out in our written response dated 22nd September. Scenario 3 of that response presented a position which demonstrated that the scheme could deliver a headline rate of 25% affordable housing, with a tenure split of 30:70 (affordable rent : intermediate housing) resulting in a Residual Land Value (RLV) of [redacted]. This RLV has been derived having been through a robust process of evidencing all model assumptions, inputs and abnormal costs. As such, Marshall considers that the appraisal represents a true reflection of the scheme viability.

Marshall notes that the Council has raised ongoing concerns about the issue of betterment. On that basis, a written opinion from David Forsdick QC is enclosed at Appendix A to this note (along with the instructions to Counsel prepared by Mills & Reeve Solicitors). Marshall believes the advice contained therein is unequivocal in confirming that it is the full costs of relocation that should be allowed for, consistent with the approach adopted to date.

Revised position

Guided by officers Marshall have explored how a headline rate of 30% affordable housing could be achieved, with a tenure split of 30:70 in favour of intermediate housing. This is illustrated in Table 1 below.

Table 1

Comments	**Headline Percentage (Market : Affordable)**	**Tenure Split (affordable rent: intermediate)**		**Residual Land Value**
Scenario 3 - as set out in ARCADIS report dated 22nd September 2015	75 : 25	30 : 70		[redacted]
Target RLV				[redacted]
Scenario 3 rebased to 30% (30:70)	70 : 30	30 : 70		[redacted]
Impact of adjusting S106 triggers for County contributions (see Appendix B for the revised triggers)	70 : 30	30 : 70		[redacted]
Revised RLV taking into account the impact of changing the s106 trigger dates				[redacted]
Shortfall in the revised RLV when compared to the target RLV				[redacted]

In light of ongoing discussions, Marshall is prepared to make an offer to accept the shortfall in the revised RLV [redacted], as outlined above, thus enabling the scheme to deliver a 30% headline rate of affordable housing with a 30:70 tenure split. This offer, and commitment to bring the scheme forward, is on the understanding that:

- The revised S106 triggers set out in appendix B are accepted;
- all other model assumptions incorporated into scenario 3 are accepted;
- there is no review mechanism in the S106; and
- the QC advice on betterment is accepted by the Council (see appendix A).

Marshall reserves the right to withdraw this without prejudice offer if any further changes are proposed to model inputs, assumptions or abnormal costs.

Appendix A – Instructions and Opinion from David Forsdick QC

MARSHALL GROUP PROPERTIES
LIMITED

WING DEVELOPMENT
ADVICE ON VIABILITY

INSTRUCTIONS TO LEADING COUNSEL TO ADVISE IN WRITING

To: David Forsdick QC

Mills & Reeve LLP
Botanic House
100 Hills Road
Cambridge CB21 PH
Tel: 01223 222235

Ref: 4006594-0010

5 October 2015

INSTRUCTIONS TO LEADING COUNSEL TO ADVISE IN WRITING

MARSHALL GROUP PROPERTIES LIMITED

Leading Counsel will find enclosed herewith copies of the following documents:

1 Opinion from Simon Bird QC with his instructions.

2 Review of the Viability Report on the Development of WING by Carter Jonas (April 2015).

3 Response to Independent Viability Assessment by ARCADIS (September 2015).

4 Letter from Instructing Solicitor to Richard Oakley at the client, dated 8 July 2015.

5 Letter from Martin Swinley of Bidwells to Chris Flood, Group Corporate Governance Manager at Marshall of Cambridge (Holdings) Limited, dated 23 June 2015.

6 Bidwells proposed methodology for calculating betterment.

Instructing solicitor is Beverley Firth, Partner with Mills & Reeve LLP. The client is the Marshall Group Properties Limited.

Introduction and WING Development context

1 The client has made 2 planning applications for a development known as "Wing" which is off Newmarket Road to the east of Cambridge. The site falls across the administrative boundary between Cambridge City Council (City) and South Cambridgeshire District Council (SCDC) – hence the 2 applications.

2 Part of the site is in current use – this is referred to as the "North Works".

3 The development is a mixed use scheme with up to 1,300 dwellings and associated infrastructure and facilities. It is a site allocated in the relevant development plans.

4 Development of Wing necessitates the demolition of buildings on site (the North Works) and the relocation of business operations. Some of the relocation will be on the client's existing land holding – but some will require land to be acquired.

5 Discussions of late with City and SCDC have focussed on matters of viability in order to settle on the appropriate level of affordable housing for the development. Leading Counsel will see from enclosure 1 that in early 2015, the client sought advice from Simon Bird QC jointly with City and SCDC in relation to what could properly be included within allowable costs.

The Question

6 Although there is substantial agreement on the elements of cost which can be allowed in the appraisal, City and SCDC have raised a question of "betterment" claiming that as the cost of relocation is to be included, so should the benefit which the client derives from that be included as "value" under a heading "betterment".

7 SCDC argue that an asset value should be included in the appraisal to reflect the fact that modern buildings will replace old on their assumption that the asset value of new premises will exceed existing asset values, particularly for those aspects of the business operating from older hangars and other premises on the North Works. Comments with regards to betterment from the Councils' advisers are set out in enclosure 2. The client has requested further justification from the Councils' advisers in terms of precedent cases and/or a proposed methodology for addressing betterment. To date, this has not been forthcoming.

8 The client's response to the suggestion of betterment is that replacement buildings will be required to adhere to current building regulations and planning policy requirements so that direct like for like replacement is not an option.

9 The Council have also taken the position (in meetings and verbally only) that the concept of 'betterment' is also important given that the routine maintenance obligations associated with new buildings will be reduced when compared with existing aged hangar buildings, affording a "benefit" to the landowner. The Client's

position is that the ageing condition of the buildings is clearly taken account of when determining the Existing Use Value of the North Works in the Bidwells Red Book Valuation. If the buildings were in better condition, the EUV would be higher and thus the Client would be seeking a higher return from the development to compensate for the loss of more valuable assets.

10 The financial viability model has been prepared in accordance with the principles of the RICS Guidance on Viability and is a cash flow model over the life of the build. The perceived increase is asset value is not addressed in the model. It is very difficult to allow for a non-cash item in the appraisal.

11 It is also noteworthy that the businesses that are to be relocated are part of the Marshall Group of Companies (including Marshall Motor Group Plc where Marshall Group is the majority shareholder). The position from Marshall Group is that the internal operating companies will not be any worse off as a result being required to relocate to facilitate the development. Rental levels will therefore be consistent with rents which would be anticipated if the development does not proceed (i.e. no change) and for a period of at least 10 years. The effect on asset value is therefore considered negligible.

12 In most cases, displaced businesses are to relocate onto Marshall owned land. As such, there is an opportunity cost of the development land which might otherwise have potential for alternative uses. Just as betterment is argued by the Council as being 'excluded', no allowance is made for this opportunity cost in the appraisal (for instance the value of building on otherwise vacant land, or for letting space to third party tenants). In a few instances where on site alternatives are not available, off site relocations (including land purchase and build costs) have been allowed for in the model.

13 Council officers have made clear that they wish to realise the wider benefits of the scheme, to include regeneration of the brownfield component of the site, and that a reduced scheme focussing on the greenfield element only in order to reduce the scheme's abnormal costs, would run contrary to the wider objectives of the adopted Area Action Plan.

14 Marshall instructed Mills & Reeve to advise on the principle of betterment (enclosure 4) and Bidwells' valuation team to devise a possible methodology for addressing the point in the absence of any identifiable precedent cases (enclosures 5 and 6 refer).

This advice has not been shared with the Council and for the reasons set out above. The client maintains the view that betterment is not something that should be reflected in the appraisal. This position is set out in the latest written response to the Council (enclosure 3).

15 Leading Counsel is asked to advise:

(a) Whether the concept of "betterment" is something which does have relevance in this context.

(b) If so:

(i) what is the most appropriate way to reflect it within the appraisal; and

(ii) does the advice differ according to whether relocation is to be on the client's existing holding or on land to be acquired.

(c) Whether there are any established precedents for reflecting betterment in asset value in planning viability cases, which may have relevance.

CAMBRIDGE EAST

ADVICE

1. I am asked to advise Marshall Group Properties Limited ("Marshall") as to whether the concept of "betterment" has relevance in the context of the approach required to relocation costs in the viability appraisal relating to the development of its land at Cambridge East ("the Land"). If it does have relevance, further questions arise. For reasons which follow, given the interpretation of the applicable policy and the relevant valuation framework, I do not think that the concept of "betterment" is relevant in this context and therefore the other questions do not arise.

The Policy

2. The Cambridge East Area Action Plan 2008 ("the AAP") adopted in 2008 is part of the development plan to which s.38(6) of the 2004 Act applies.

3. Policy CE/33 provides that:

> ***"The appropriate level of contributions sought from the development will take into account costs which fall to the development, including relocation of the airport and associated activities and elements of the North Works site."***

4. Relocation is a fundamental part of the AAP and the allocation cannot be delivered without it[1]. This is not a situation where the policy envisages most existing uses being extinguished – they are to be relocated. It necessarily follows that the development has to facilitate and secure the identified relocations. This is thus a reinstatement situation.

5. The policy means what it says: *Tesco v. Dundee.* It is not necessary or appropriate to introduce concepts from other contexts (such as betterment in the CPO setting or offsetting of damages in tort law) to construe it[2]. Even if I am wrong on this latter point, it is not at all clear what legal principle could be relied on to off-set any capital value enhancements here against costs which the landowner has to incur. Even in an equivalent reinstatement situation under rule (5) of section 5 of the Land Compensation Act 1961 (which does not apply here) there is no offset for the existing building being relatively obsolescent compared to the new replacement[3].

6. Fundamentally, under the policy as under rule (5) the focus is on the relocation *costs* which fall to the development – not on the possible, inchoate and potentially unrealisable capital *value* to the relocated landowner. The question, therefore, is what will it cost the development to provide alternative premises and relocation so as to allow the development to go ahead? I understand that figure to be (largely if not wholly) agreed.

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[1] although (on the margins) there is some degree of flexibility as to what should/should not be relocated. I do not go over ground covered in the Advice of Simon Bird QC dated 20th January 2015.

[2] except to the extent to which such concepts are incorporated by reference. Of course here this is not a CPO situation or a situation where the threat of CPO will secure the relocations. Compensation does not fall to be addressed under the compensation code.

[3] Any offset is limited to the extent of disrepair in the existing building which would have to be made good to allow the existing building to continue to function for the use: see e.g. *Cunningham v. Sunderland CBC* (1963) 14 P&CR 208 and Zetland Lodge of Freemasons v. Tamar Bridge Joint Committee (1961) 12 P&CR 326.

7. The words "take into account" can mean either "by reference to" or "having regard to". I will assume that the latter (weaker) formulation is the correct one here, but even on that basis there is nothing in the facts as I understand them which would appear to justify anything other than the full relocation costs incurred being treated as a deduction in the assessment. The policy will necessarily have been formulated on the unstated assumption (which I also make) that the earlier stages of the valuation and, in particular, the approach to land values is consistent with the inclusion of relocation costs – in other words (as dictated by the overall policy framework) this is a reinstatement approach[4] rather than simply compensation for the land acquired required. Application of this assumption avoids the risk of double counting deductions in the valuation and ensures that the valuation follows an internally consistent and coherent framework. On that basis the costs of relocation should feed directly into the viability appraisal. That seems to me to be consistent with the basic purpose of the policy – namely to secure the necessary relocation through charging it to the development.

8. Those advising the Councils have suggested, nonetheless, that because the existing buildings will be replaced with new modern facilities there will be betterment to the landowner: see para 4.5.4.2 of Cater Jonas report dated April 2015. "Betterment" is principally a *statutory* concept within the compensation code. In that sense, it does not apply here. What I think is being said is that because the new buildings may have lower maintenance costs and longer lives than the existing, the landowner will, following relocation, be in a better capital value position than currently. As a result, so the logic goes, the development should require that the landowner accounts for that "improvement" in possible capital value by contributing to the costs of relocation thus reducing the burden on the development (even though he has no intent or ability to realise that capital value). That would be a surprising result given the basic facts here – it would be requiring a landowner to move *and* to pay for the claimed improvement whether he sought or benefitted from that improvement in capital value or not without any statutory authority for the deduction and without any indication in the words used in the policy that this was their intent. I note that such a result would be inexplicably *inconsistent* with the position under the statutory compensation code rule (5) for reasons already addressed.

9. I think it would require clear words for the policy to have that effect. In my view there is no indication in the words used that the costs falling to the development are anything other than the full costs of relocation.

David Forsdick QC

13th October 2015

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[4] Clearly the statutory/case law requirements for compensation being based on "equivalent reinstatement compensation" are not met but the effect of the overall policy framework is to envisage reinstatement rather than extinguishment and the policy is designed to ensure this is reflected in the compensation approach. Even in a statutory context, there is no deduction from the equivalent reinstatement compensation for the comparative age of the new and the existing building.

Appendix B – Revised S106 triggers

Revised assumptions on S106 triggers as follows:

S106 item	Original trigger	Proposed trigger
County Council contribution for secondary school provision	10% on occupation of 300th dwelling 30% on occupation of 500th dwelling 30% on occupation of 700th dwelling 30% on occupation of 900th dwelling	40% on occupation of 500th dwelling, 30% on occupation of 800th dwelling, 30% on occupation of 1,000th dwelling
County Council contribution towards Chisholm Trail cycle bridge	Prior to occupation of 150th dwelling	Prior to occupation of 300th dwelling
County Council contribution for Newmarket Road improvements	Prior to occupation of 750th dwelling	Prior to occupation of 1,000th dwelling

ANNEX 2 – RESPONSE TO DETAILED COMMENTS RAISED IN THE CARTER JONAS LETTER OF 14TH OCTOBER

2. Detailed comments on the submitted appraisal

2.1 Unit sizes and values

The submitted planning application makes an allowance for up to 1,300 residential dwellings. The masterplan has been tested through proving layouts by our masterplanners Pollard Thomas Edwards (PTE). With the unit sizes proposed, a scheme for 1,300 dwellings can be achieved, whilst delivering dwelling sizes in accordance with London design Guide minimum dwelling space standards, which are acknowledged as being more generous that HCA standards. This includes ensuring all homes will meet the construction standards of Lifetime Homes. This aspiration has been clearly stated since the application was submitted in December 2013.

Although dwelling sizes are not prescribed in the planning application documents, the proposed mix is clearly articulated in the viability model (first issued November 2014) and market advice has been sought from both Savills and Bidwells to ensure the assumptions reflect the expectations of the market.

As Carter Jonas note in their letter, *"it is at the discretion of the applicant to determine the unit sizes"* and Marshall has remained committed throughout to a high quality development, with homes that are flexible to meet the needs of their occupiers over the life of the development.

In terms of values, whilst we note the comment that values on the Redrow scheme at Hauxton are achieving up to £420 sq ft, it is simply not the case that these are directly comparable for a range of reasons, including the relative attractiveness to the market of the south side of the City and the fact that the Wing site is located adjacent an operational airport, Newmarket Road and adjoins some of the more deprived wards in the City. Marshall intends to stand by Savills advice of a blended rate of £410 sq ft which is current and takes into account the location of the development on the eastern side of the City.

2.2 Ground rents

In response to Carter Jonas query regarding the level of ground rent applied in the model. We would refer to the Carter Jonas' report, dated April 2015 Rev C, in which it states in section 4.3.5 that *"ground rent assumptions used by the applicant at an average of [redacted]/unit per annum is realistic"*. We are unclear as to why this position has changed and consider the position to be robust and reasonable.

2.3 & 2.4 Affordable rent & intermediate residential income

Since the viability model was first issued to the Council in November 2014, there have been many discussions with the Local Authorities about the approach to benchmarking the assumptions on affordable housing revenues in the model.

Initial discussions with the Council's Housing Team (Sarah Lyons) indicated that BPHA would be an acceptable Registered Provider to provide a benchmark figure for viability purposes. BPHA are active in the Cambridge market and are very familiar to South Cambridgeshire District Council.

The initial offer received from BPHA dates back to October 2014, and this has been refreshed in the light of changing market conditions which have a bearing on the intermediate housing values (as house prices have increased), as well as changes in circumstances, including the Budget announcements by the Chancellor in July 2015, which have reduced rents for social housing.

In light of the July Budget, Marshall asked BPHA to refresh the proposal in light of the announcements on rental income. The revised offer was received from BPHA on 24th August 2015, following Board decisions within BPHA about how to address the Budget implications.

Following further discussions with BPHA in light of the Carter Jonas letter, BPHA have confirmed that the offer they have put forward is robust and they stand by the offer. Steve Morris (Regional Development Director) has confirmed he would be prepared to discuss the assumptions with officers if this is deemed necessary. We can provide contact details if required.

Marshall has also approached other Registered Providers including London & Quadrant, Flagship and Rent Plus, but given the stage of the project, it has been difficult to persuade them to put forward offers purely for viability purposes due to the resource requirements involved. The only offer obtained (from Rent Plus) was well short of the equivalent offer from BPHA.

On that basis, Marshall believe that at the outline application stage, use of a market tested figure from BPHA is a robust approach to adopt and we stand by the figures included in the appraisal.

3.2 Non-residential income

We note that in the first paragraph of the Carter Jonas letter it states that they have not reviewed the Arcadis report. In this report, on page 11 it gives detail to the valuation of the petrol station. Please see extract below:

"Marshall Group has informed us that negotiations are underway with a petrol filling station provider and that their preferred method of occupation is a ground rent. It has been proposed that a standard ground rent for a site of this nature is [redacted] per annum with a lease length of 25 years therefore all construction costs for this element have been removed from the model."

To achieve a value of [redacted] the passing ground rent has been multiplied by the duration of the proposed agreement.

3.3 Developers Margin

In response to Carter Jonas' query in respect of the Commercial Developers Margin of [redacted] we can confirm that this is charged on non-residential build cost only. This cost is in the sum of [redacted] of which [redacted] is [redacted] as allocated in the model.

3.4 Build Costs

Marshall has sought expert advice from ARCADIS which has informed the assumed build cost of £137 sq ft, which is evidenced in our September 22nd Report. If anything, the true figure is likely to be higher than this based on discussions between Marshall and a number of leading developers who are active in the City. Marshall is satisfied that this is robust, and if anything at the optimistic end of what could be achieved. Our expectation would be that a developer would seek to demonstrate a higher build cost in the viability appraisal.

3.5 Basement Parking

With respect to the necessity of basement parking queried by Carter Jonas, we would again refer them to the Arcadis report (September 2015). The extract below is taken from page 10 of the report.

"Following discussions with Officers, Marshall tasked PTE and Arcadis to review the position with regards to car parking requirements and the need for, and cost of, any underground car park.

The analysis has confirmed that an underground car park is required for at least 150 spaces. The Design and Access Statement submitted with the planning application indicates the potential for a car park of up to 300 spaces. PTE have confirmed that a car park of this size is not required, and that the size can be reduced by allowing parking around the edge of Beta Square. However, below a threshold level of 150 spaces, the number of dwellings needs to

be reduced in order to provide parking courts and other off street parking arrangements. PTE's analysis indicates that the scheme would need to reduce by 43 dwellings (31 two and three bedroom houses, 12 no. one/two bedroom flats). This is not considered viable when compared with the construction cost of the car park."

The cost allowance for the basement parking has been included at a rate that sits in the range of costs currently being seen by Arcadis (£25,000 - £45,000 per space) on schemes of a single storey with a number of variables including height, efficiency, substructure solution, ground conditions etc. Given the early stages of Wing the basement parking has not been designed in detail and therefore in costing the basement for the purposes of the viability model at £32,000 per space we have allowed for a cost inclusive of substructure and ventilation.

3.6 Development Management Fee

It has been raised by Carter Jonas that they would like comfort that the allowance in the model for the Development Management Fee does not cause a double counting error when professional fees allow for a QS and site management. In response to this query, we have asked Arcadis to confirm the allowances in the model. We have been informed that there is no double counting error in the model and each of the inputs are reasonable for the house build cost and are representative of the percentage allowance modelled by house builders and developers on other strategic land sites where there are a range of product types requiring variations in design which attract additional fees. The DM fee reflects the requirement of an overarching DM in the project whether that be Marshall or a developer.

3.7 Site Wide Infrastructure

Carter Jonas have raised queries with the Site Wide Infrastructure costs. Noting that they admit that they have not reviewed the Arcadis Report, we include this sections from the report below.

"The Arcadis infrastructure cost plan has been updated taking into consideration the comments provided by Silver. One item questioned by Silver was the risk cost which is based on a detailed risk review and workshop, attended by the client and key consultants. Given that time has moved since the initial review and workshop, and the comment raised by Silver, it was agreed that a further risk workshop would be held. The outcome of the second risk workshop has reduced the risk allowance by [redacted] or [redacted] when compared to the original figure reviewed by Silver.

The table below provides a breakdown of the costs modelled within the infrastructure cost plan taking into consideration the review undertaken by Silver DCC. Of the total [redacted] reduction suggested by Silver [redacted] has been accepted and agreed by Arcadis. Arcadis have also taken the opportunity to index the infrastructure cost plan to current prices (Q2 2015). The indexation of costs has resulted in a [redacted] uplift in costs when compared to the model reviewed by Silver. Overall strategic infrastructure costs have decreased by [redacted] (after cost indexation) when compared to the original cost plan reviewed by Silver.

An annotated version of the below table is included in Appendix F which provides commentary on the reason for the changes on the Arcadis version."

As can be seen in the submitted report Arcadis have reviewed the Silver report in detail and accepted those points which are considered reasonable.

3.8 Relocation Costs and GRE

We are unclear as to the source of the [redacted] given the relocation costs are deemed to be broadly aligned in terms of the Bidwells relocation costs report and advice from cost consultants Silver.

With regards the point on the land acquisition cost, we have addressed this under point 1 and consider that it is absolutely legitimate to include the full cost of relocations (including land) otherwise the scheme cannot come forward in accordance with the QC advice obtained.

It is noted that there is a difference of opinion between Silver DCC and Mott MacDonald with regards to the likely cost of the Aircraft Ground Run Enclosure, but our position has been clearly set out in the 22nd September response on this matter.

3.9 Cost of Equity / Debt funding

We note the comments made regarding the approach to reflecting the cost of equity, but that the debt funding costs are low. Carter Jonas accept "that the two points would balance themselves out." Marshall consider this point is now resolved.

ANNEX 3 - Draft Wording of Proposed Cascade Mechanism (prepared by Mills & Reeve)

Approach to Affordable Housing Delivery

Market forces should be used to assess the demand for the Affordable Housing. As such, the cascade mechanism should be triggered where an RP is unwilling to purchase the Affordable Housing Units ("AHUs") within a development parcel at the equivalent value attributed to those units in the viability assessment underlying the application.

Starting Point

1.1 30% of the Residential Units in a Phase are to be Affordable Housing of which, 30% will be Affordable Rent Units and 70% will be Intermediate Units.

1.2 An Affordable Housing Scheme ("AHS") will be submitted to and approved by the Council for each development parcel within a Phase at the reserved matters stage for that development parcel. The AHS will identify the type, size, number and location of the AHUs in that development parcel. The AHS shall be broadly consistent with the requirements of 1.1 above and if lower, will demonstrate how the requirements of 1.1 will be achieved across the entire Phase.

Cascade Options

1.3 If developer is unable to exchange contracts with an RP for the transfer and construction of the AHUs in a development parcel then:

- Stage 1: If feasible, the developer shall propose an alternative AHS for that development parcel which: reflects the demand from an RP; achieves the same level of AHUs in that development parcel; and secures the Affordable Housing income for those AHUs identified in the appraisal underlying the application (adjusted by indexation). The proposal may, for example, identify alternative types of AHUs or starter homes (which for the purposes of this cascade shall be construed as being affordable housing).

- Stage 2: If stage 1 is not feasible or acceptable to the Council, the developer may propose an alternative AHS for the development parcel which achieves the Affordable Housing income for those AHUs identified in the appraisal underlying the application (adjusted by indexation) but which contains an increase in Affordable Rented Housing and as a consequence a reduction in the overall quantum of AHUs in that development parcel. If the AHS is approved by the Council, the overall percentage of Affordable Housing to be delivered across the development shall be reduced accordingly;

- Stage 3: As an alternative to Stage 2, the developer may offer the AHUs in that development parcel to the Council at a price reflecting the Affordable Housing income for those AHUs identified in the appraisal underlying the application (adjusted by indexation).

- Stage 4: As a last resort, those AHUs are to be treated as market housing units and the developer is to pay an off-site affordable housing contribution to the Council in lieu of the provision of Affordable Housing on that development parcel. The contribution shall reflect the difference between the open market value of those dwellings which would have been AHUs and the value that would have been realised if those units were sold to an RP in accordance with the

Affordable Housing income identified in the assessment underlying the application (adjusted by indexation). The overall Affordable Housing requirement will reduce accordingly.

Appendix B

Carter Jonas

14 October 2015

6-8 Hills Road
Cambridge
CB2 1NH

Mr P Mumford
Team Leader, New Communities
South Cambridgeshire Hall
Cambourne Business Park
Cambourne
Cambridge CB23 6EA

Dear Paul

WING REAPPRAISAL BY E C HARRIS

Further to the issue of the updated scheme appraisal by EC Harris and our recent meeting, we write as requested to give all three Councils advice in respect of the revised appraisal and the current position with regard to the viability of the scheme. We have, as discussed, in the time available just been able to look at the macro issues the revisions to the appraisal throw up. At this stage we have not reviewed the Arcadis report, as until the base appraisal is agreed we cannot give recommendations with regard to quantum, mix and tenure of the affordable housing.

1. Points of principle

1.1 The appraisal shows a cost of [redacted] for the relocation costs including the engine running bay. Whilst it is agreed that this can be taken into account and Counsel has opined on this matter, there has been no offset allowed for the value of the buildings created through the relocation process. We are still of the opinion that such value should be taken into consideration because to do otherwise would allow the land owner not only to recover the benchmark land value (Market Value) for the site, but have the benefit of new premises on the new site as well.

This is interlinked with the principle of 'Benchmark Value' in viability appraisals. Clearly Marshalls should expect as a minimum, the Market Value of their site which they say is [redacted] (Albeit we have concerns as to whether this value reflects the full effect of the Engine Running Bay on some of the land) However, the Area Action Plan states: *"The appropriate level of contributions sought from the development will take account costs which fall to the development, including the relocation of the airport and associated activities and elements of the North Works site".*

So does this imply that Marshalls' reward for the land (the Benchmark Land Value) should equate to the Market Value of their site, or should it be sufficient to cover for the costs of relocation, or both? The point here is that the costs of relocating the existing buildings are about double their Market Value. This suggests that there is significant 'betterment'.

Based on the applicant's previous viability submissions, we have advised that if full relocation costs are included in addition to the Market Value of the land, then the scheme will not be viable.

We would recommend that Counsel be asked to give an opinion on this and whether the value as well as the cost of the relocated premises should be taken into consideration in coming to a conclusion about the viability of the scheme. This matter was not covered in Counsel's original written opinion.

1.2 If the final position with regard to viability is such that a non-policy compliant affordable housing offer is initially accepted, then the Councils should consider a review mechanism prior to the implementation of each sub-phase of the scheme. We would suggest that no phase for a viability review is greater than 200 units and that the trigger for the review is the sale or occupation of 150 units on the preceding phase.

1.3 By way of further explanation, we attach a separate summary sheet on relocation costs/viability.

2. Detailed comments on the submitted appraisal

2.1 Unit sizes and values

Firstly we would note, as we have done on previous occasions, that the unit sizes particularly in reference to the 2 and 3 bed house types, are far larger than normally encountered in the market. This is having a negative effect on the viability of the scheme because there is always a 'glass ceiling' for the price that someone is willing to pay for a particular unit type. This has also thrown up the anomaly that the price per ft^2 of a 3 bed is being shown lower than that for a 4 or 5 bed, despite the Savills' research demonstrating to the contrary in terms of comparable evidence on other sites.

Whilst it is at the discretion of the applicant to determine the unit sizes, the Councils need to be aware of the detrimental impact this is having, and the need to consider whether this is a policy-driven imperative for the scheme.

Another development which has been recently launched by Redrow is at Hauxton Meadows on the former Bayer site outside the City boundary to the south. Whilst it is recognised that there are differences between these two schemes, at Hauxton sales are at about £420 p sq ft, which suggests that the blended £410 p sq ft at WING is conservative.

2.2 Ground rents

We are satisfied with the yield and costs applied, however the average rent per annum at [redacted] seems very low and we would anticipate a figure more in the order of [redacted] per unit is relevant in the current market for Cambridge.

2.3 Affordable rent residential income

The rate used of [redacted] when expressed as a percentage of OMV, has reduced to [redacted] Again this seems very low, although we acknowledge the changes just introduced, requiring rents to be reviewed to below rather than above the rate of inflation, which will reduce value. We appreciate this is based on an indicative offer from BPHA, although there is little justification to this in their brief email.

2.4 Intermediate residential income

We would note that the rate used at [redacted] is giving a percentage of OMV at [redacted] This would seem slightly high and we would recommend checking the affordability of the units concerned.

2.5 Non-residential income

Almost 80% of the commercial income is attributable to the supermarket. The proposed valuation based on [redacted] yield is considered to be reasonable. We would like to seek clarification on the [redacted] valuation for the petrol station in due course.

2.6 Developer's margin

We are content with the percentages used, albeit we believe the commercial profit calculation should be revisited as it does not seem to be correct – the figure should be higher.

2.7 Build costs

The new base build cost rate applied by E C Harris at £137/ft² looks high, however we note that it is inclusive of external works and therefore would be necessarily higher than the median BCIS rate.

2.8 Basement parking

We note the cost has increased to £32,000 per space, which seems excessive. This is a total cost of £4.8M to the scheme, firstly we would query whether the Council see the need for this type of parking provision and secondly if it does, we would recommend the figure is checked by Silver DCC as above.

2.9 Development management fee

We note this has been allowed at [redacted] costs but we would also note that the professional fees include [redacted] for a QS and [redacted] in addition for site management. Whilst we have already confirmed we are not against the principle of a development management fee, we would ask that the applicant confirm there is no double counting in this respect. We would further point out that on multi-phase developments such as this it is common for the principle applicant to co-ordinate and remain liable for the payment of S.106 costs in the future, and the development management fee is often used to cover the cost of this co-ordinating function.

2.10 Site-wide infrastructure

We note that the current appraisal shows a figure of [redacted] and whilst this reflects some of the savings identified by Silver DCC, it has been increased by indexation from the time of the last EC Harris submission. We would note that the Silver DCC report was issued in August of this year and therefore we believe that the [redacted] of savings that they have identified are still applicable with indexation from that date.

2.11 Relocation costs and GRE

We note that there is a difference of [redacted] between the costs identified by Silver and EC Harris. The applicant needs to explain why this cost saving is not relevant. Further, there is an allowance of [redacted] for land acquisition to relocate the existing premises and this reinforces the point made at 1. above about the need to include the value of the replacement premises as well as the cost.

2.12 We note that within the funding model equity funding costs of [redacted] have been allowed, using a return rate of [redacted] We do not believe this is the right way for this to be presented, as equity providers are normally rewarded by dividends from the profit the scheme creates. Having said

that, we believe the debt funding costs are low and therefore the two points would balance themselves out.

3. S.106 Costs

3.1 You have advised today that the bulk of the S.106 costs at £28,234,269 are now fixed between the parties, however the applicant has queried the validity of the contribution for the Newmarket Road corridor (£2,27M) and the cycle bridge (£475,000). When presenting our final report we will be happy to provide appraisals with and without these figures, but in the first instance need your confirmation that is the approach you wish to take.

We trust the above is of help in briefing members, and your further discussions with Marshalls before we are requested to complete our report for the planning committee.

Yours sincerely

A M LEAHY
Bespoke Property Consultants

M HALLAM
Carter Jonas

Appendix C

Appendix D

Review of the Viability Report on the Development of WING

On behalf of South Cambridgeshire District Council and Cambridge City Council

April 2015
Rev C

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maximising development potential

2.0 Executive Summary

2.1 We have reviewed the report by E C Harris (ECH) dated March 2015 and concluded that the main issues relating to the viability of the scheme are the relocation costs used in the applicant's appraisal and the value of the replacement buildings being relocated, which has an effect on the benchmark land value to be used for the scheme.

2.2 CJ have carried out an independent appraisal of the scheme and the results of this are shown at Appendix A.

2.3 We have reviewed the inputs and assumptions used by ECH as set out in Section 4 below and found them on the whole to be reasonable, with the exception of

a) The cost allowances for certain items within the relocation costs, which are provisional sums due to lack of design and technical detail at this stage. Investigation of these costs would require specialist consultants.

b) The applicants have included the cost of the relocated buildings, but not included a value for these premises. This is skewing the appraisal and does not take account of the betterment achieved with the delivery of the new buildings for the land owner.

c) The applicants have provided a benchmark land value for the scheme at [redacted] from which we accept the value of the existing buildings on the site, we have reservations as to whether the valuation of the un-developed land is compliant with RICS Guidance Note 94/2012.

2.4 CJ have carried out a summary appraisal which reflects the applicant's build costs and sales values which derives a residual land value of [redacted] (assuming the cost of the relocated buildings equals their value). This has been carried out with the provision of 40% of affordable housing with a tenure mix of 60% affordable rented and 40% intermediate, together with S.106 contributions of £26m. This residual value is above the benchmark and therefore viable.

2.5 The applicant has been asked to justify the values they have put forward and provide more evidence to support their position. We would note that the benchmarking provided within the ECH report is anonymous due to reasons of confidentiality, therefore we are able to only give this limited weight as we have no details as to whether the data used is comparable.

2.6 The applicant has offered 40% affordable housing with a 50/50 tenure split between rented and intermediate, albeit they say that this is unviable. We have concluded that such an offer is reasonable and viable, when taking account of the replacement value of the relocated buildings. That said, this conclusion is still reliant on the relocation cost provided by the applicant being accurate, which we are unable to verify without investigation by specialist consultants.

2.7 Should the Council be minded to grant consent with the affordable housing tenure mix and S.106 contributions as put forward by the applicant, which is not policy compliant, then we would recommend a viability review mechanism is included in the S.106 agreement.

2.8 If the Council's intention is to ensure that the scheme is started in a timely manner then we would suggest the review is carried out if the first phase has not reached slab level on 20 no plots within two years of consent being granted.

2.9 The review mechanism would be on the basis of seeing if the scheme can achieve a policy-compliant tenure mix.

2.10