WELBORNE GARDEN VILLAGE

Planning Viability Review

Addendum Report

July 2021

CBRE

Welborne Garden Village – Planning Viability Review July 2021

CBRE has been instructed by Fareham Borough Council (FBC) to undertake a review of the further amendments to the outline planning application submitted by Buckland Development Ltd (BDL), issued on 8th June 2021, in relation to Welborne Garden Village (WGV).

Reliance

This report is addressed to Fareham Borough Council only and should not be reproduced without our prior consent.

Background

CBRE previously advised FBC on viability statements prepared by BDL in relation to the viability of WGV. This culminated in the approval of the planning application for WGV in October 2019. CBRE undertook a detailed review of the proposals put forward by BDL in the lead up to the October 2019 planning decision and concluded, on viability grounds, that:-

- The scheme should not be liable to pay the Community Infrastructure Levy (CIL)
- The developer contribution towards M27 Junction 10 costs is capped at £20m
- Affordable housing for the first 1,000 units should be 10%
- The affordable mix for the first 1,000 units is split 50/50 between affordable/social rent and intermediate tenures
- The scheme is unable to provide Lifetime Homes or Passivhaus for the first 1,000 homes

In addition to the above, terms were agreed for a viability review mechanism. The purpose of this was to monitor and review the viability of the scheme over time so that if viability improved it could be possible for the policy requirements to be met either partially or in full. The key terms of the viability review mechanism were as follows:

- First review to be completed following completion of the 1,000th residential unit and occur at a frequency of 750 unit completions thereafter.
- The review will be in accordance with the agreed financial model and a number of agreed financial parameters. Over time, the actual known costs and revenues will replace the original forecasts.
- In addition to 750 unit phase reviews, BDL will provide an annual financial return statement as part of the monitoring arrangement with FBC.
- Any additional grant funding received may trigger a standalone viability review.
- Affordable quantum and tenure, Lifetime Homes and Passivhaus will form part of future viability reviews. FBC will have the ability to adjust and prioritise its requirements in relation to these items should the scheme not be able to afford them all.

An important part of the viability position at the time was how the new Junction 10 of the M27 would be funded. The junction must be provided to enable more than 1,160 units to be occupied due to highway constraints. At the point of the planning application determination, it was highlighted that there was a funding gap for the estimated £80-90m costs of the Junction 10 scheme. Funding had been allocated as follows:

- £20m developer contribution
- £10m of Housing Infrastructure Funding provided by Homes England, unconfirmed
- £14.15m of Solent Local Growth Deal funding allocated by the LEP
- £14.9m of Solent Growth Deal funding retained by the DfT

Given that all the funding for the junction was not in place, a planning condition was imposed for BDL to revert back with a confirmed junction funding strategy before any development, other than the Junction 10 works, could commence.

Planning Viability Review – January 2021

Further to the approval of the planning application in October 2019, BDL submitted an updated planning viability statement, dated 17th December 2020, in relation to WGV. This was driven by the requirement for BDL to provide clarity over the funding strategy for the infrastructure works which relate to Junction 10 of the M27.

The Junction 10 scheme delivery cost was estimated to be in the region of £75m, following the progression of a more cost-effective design.

Of the £14.9m Solent Growth Deal funding retained by DfT, £5.5m has been advanced to progress scheme design. The remaining Solent Growth Deal funding retained by DfT, and the £14.15m locally earmarked Solent Growth Deal funding has been reallocated to other infrastructure projects in the LEP's pipeline that could spend the funding before the end of March 2021.

Discussions with Central Government resulted in an increase in the offer of Housing Infrastructure Funding (HIF) from £10m to £30m. However, even with the scheme costs reducing and the HIF offer increasing, a funding gap of £20m remained. To enable the scheme to be brought forward BDL proposed to increase their total junction contribution to £40m.

CBRE was instructed by FBC to undertake a review of the updated planning viability statement submitted by BDL. Following a detailed review of the revised proposal, CBRE was of the opinion that the revised proposition put forward by BDL was reasonable on viability grounds and that as a result of making an additional £20m contribution to the junction:-

- Overall, the scheme produces a profit of 1.5% based on today's costs and values
- The developer contribution towards M27 Junction 10 costs is capped at £40m
- The scheme should not be liable to pay the Community Infrastructure Levy (CIL)
- Affordable housing should be 10% minimum
- The affordable mix is split 50/50 between affordable rent and intermediate tenures but this should be re-assessed during future viability reviews
- The scheme is unable to provide Passivhaus or Lifetime Homes but this should be re-assessed during future viability reviews
- Viability reviews should be held at 3,000, 3,750, 4,500, 5,250 and 5,750 dwellings
- It is appropriate to have two recovery mechanisms – HIF repayment & Planning viability review
- The use of 80% of any surplus above 20% profit on cost to repay the HIF funding and the developer to retain 20% of any surplus is reasonable.
- The Profit at 20% on GDV proposed for the Planning viability review is in line with planning guidance
- The 50/50 profit share proposed for the Planning viability review is reasonable

Current Position

FBC submitted a recommendation to the full Council on 7th June 2021 that the area of Welborne be nil rated under the Revised Community Infrastructure Levy (CIL) Charging Schedule. This was approved on 10th June 2021 on the basis that the imposition of CIL at Welborne, in addition to the site wide infrastructure works required, would impact development viability.

The M27 Junction 10 scheme delivery cost is now estimated to be in the region of £81m. Discussions with Central Government have resulted in an increase in the offer of funding to £42m. This comprises £41.25m of Housing Investment Grant (HIG) funding and £750,000 Capacity Funding from Homes England. CBRE is aware that negotiations on this are progressing at pace and although there is a reasonable prospect of this funding being available for Welborne Garden Village, the funding remains subject to completion of various documents namely,

the S106 Agreement and the Grant Determination Agreement (GDA) between Homes England and Hampshire County Council. In addition, FBC is required to enter into a Memorandum of Understanding (MOU) with Homes England which relates to HIG recovery, recycling and the monitoring and reporting of housing output at WGV.

CBRE has been advised that as part of the proposed agreement Homes England is seeking to bring forward the first planning viability review to 2,000 homes with subsequent reviews to take place upon completion of the 3,000th, 4,000th, 5,000th and 5,800th home. This would be in addition to the review being proposed by BDL upon receipt of confirmation of any cost overruns which may result in a reduction of the number of affordable housing units to be delivered at WGV.

To enable delivery of the Junction 10 scheme BDL has proposed to increase their total junction contribution to £40m and to bear any cost overruns up to a maximum of £10m – equating to a total potential contribution of £50m. If the HIG funding is made available and the scheme costs remain at or below £81m, this proposition would address the funding requirement.

The potential increased contribution from BDL could impact the overall viability of the scheme, particularly the provision of affordable housing, and this has led to BDL seeking to amend the previously approved viability position in the event that the £10m cost overrun is required. Within its revised viability statement BDL has set out its proposed viability position as follows – it should be noted that the some of the statements are as per the consented scheme and others are updates as a result of the potential requirement to make an additional £10m contribution to Junction 10.

Proposed BDL Financial Viability Position

BDL has stated that should there be a requirement to contribute an additional £10m, taking total developer contribution to £50m, to cover any exceptional cost overrun during the construction of the junction, this will further impact the viability of the scheme. In order to maintain a return of 1.5% profit on both cost and Gross Development Value (GDV), down from 14.4% profit on cost (12.6% profit on GDV) level that the scheme was showing in October 2019, the number of affordable housing units may need to be reduced below the previously agreed level of 10%.

In order to maintain current levels of profitability, BDL has proposed that any cost overrun contribution should result in a reduction of one affordable housing unit for each £62,500 increment of overspend. If the additional contribution of £10m is required in full this will result in a reduction of 160 affordable housing units throughout the development period.

CBRE has been asked to advise FBC on the reasonableness of the proposed changes and our findings are detailed below.

CBRE REVIEW OF BDL'S PROPOSED CHANGES

CBRE has historically undertaken extensive reviews of the financial appraisals prepared by BDL including detailed reviews of the supporting cost and value information. Our findings are contained in the Site Wide Viability Report and Addendum report prepared for the October 2019 planning committee and the subsequent planning viability review undertaken in January 2021.

In providing the updated financial appraisal, BDL has not made changes to the cost and value assumptions nor have they considered reducing the £288m of site-wide infrastructure costs set out in the Infrastructure Delivery Plan which, for the avoidance of doubt, does not include the contribution to the M27 Junction 10 improvement works. The key changes include the additional £10m contribution towards the junction works and a reduction of the total number of affordable housing units from 600 to 440 units. Whilst a review of the updated financial appraisal has been undertaken to determine the extent of BDL's proposed amendments and the reasonableness of its inputs and assumptions, CBRE has not undertaken an audit of the functionality of the financial model itself. It is assumed that the formulas are correct and that the model outputs can be relied upon.

BDL have sought to determine what impact any cost overrun contribution may have on scheme viability. If the developer's contribution is to be increased to £50m from the current cap of £40m whilst maintaining a profit of 1.5%, BDL has indicated that a reduction of 160 affordable housing units, to a total of 440 units, is required; this equates to an overall reduction of 2.7% in affordable housing provision across the development lifecycle.

Based on today's costs and values, the current low levels of profit indicate that any substantial increase in costs will lead to a deficit and impact the viability of the scheme. Furthermore, it is important to note that current levels of profitability without the cost overrun is significantly below market norms and a total developer contribution of £50m is significantly higher than most developers would provide under these circumstances.

The proposed mechanism of reducing affordable housing provision by one unit for each £62,500 increment of overspend is a factor of the maximum additional contribution of £10m for any cost overruns divided by the overall reduction of the affordable housing units. Given that the timing and potential for cost overruns are unknown at this stage, this appears to be an equitable way of determining a reduction in order for the development to commence.

In addition, it is likely that the junction 10 works are due to take place during the earlier stages of development and perhaps even prior to the initially proposed viability review at 2,000 homes. The earlier the requirement to provide the additional contribution of up to £10m, the more significant the impact to affordable housing delivery as the scheme could incur increased finance costs.

Any reduction of affordable housing to be agreed with BDL will be subject to scrutiny at each viability review and revised upwards if actual costs and values show that the scheme is more profitable than currently predicted. Notwithstanding this, previous sensitivity analysis undertaken by CBRE indicated that it takes circa 15 years for the scheme to break even and that most of the profit is delivered towards the back end of the scheme.

Overall, it appears that proposed mechanism for reducing the number of affordable housing units to a minimum of 7.3% is reasonable if BDL is required to contribute additional funding over and above the existing cap of £40m.

CONCLUSIONS

BDL previously agreed to increase its contribution to the junction to £40m. CBRE's previous report to Planning Committee stated that, "if the BDL contribution towards M27 Junction 10 costs is increased beyond £20m it will adversely affect the viability of the scheme and the ability to meet the various policy requirements". Subsequent viability modelling undertaken demonstrated that BDL is unable to provide more than £40m, without further policy concessions.

CBRE is of the view that the revised proposition put forward by BDL is reasonable on viability grounds. We therefore concur with BDL that as a result of bearing additional cost overruns to a maximum of £10m, taking the total developer contribution to £50m, in relation to the proposed junction: -

- Overall, the scheme produces a profit of 1.5% based on today's costs and values
- The developer contribution towards M27 Junction 10 costs is capped at £40m with a potential extra £10m for cost overruns
- Affordable housing should be 10% minimum until such a time that cost overruns have been confirmed
- A reduction in affordable housing provision by one unit for each £62,500 of additional contribution is reasonable
- Any reduction in the provision of affordable housing should not fall below a minimum of 7.3% in the event of any cost overruns
- The affordable mix is split 50/50 between affordable rent and intermediate tenures but this should be re-assessed during future viability reviews

- The scheme is unable to provide Passivhaus or Lifetime Homes but this should be re-assessed during future viability reviews
- Viability reviews should be held at 2,000, 3,000, 4,000, 5,000 and 5,800 dwellings
- It is appropriate to have two recovery mechanisms – HIG repayment & planning viability review. HIG repayments will precede the planning reviews and all payments will be made in line with the proposed profit sharing arrangement agreed in January 2021.