



## Appeal under Section 78 of the Town and Country Planning Act 1990

De Paul House, 628-634 Commercial Road, London E14 7HS

Proof of evidence of Anthony Lee PhD MRTPI MRICS

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# 1 Qualifications and experience

- 1.1 I, Anthony David Lee BSc (Hons) MSc (Econ) MA (TP) PhD MRTPI MRICS confirm that:
- 1.2 I am a Senior Director and Head of UK Development Consultancy at BNP Paribas Real Estate, one of the UK's leading real estate consultancies with fifty regional offices in addition to its London offices.
- 1.3 I am also the Director in charge of the Development Viability Team in the London office with responsibility for the viability service across London, the South and the East of England. I have advised London boroughs, the Greater London Authority, landowners and developers on the viability of numerous major mixed-use developments in London and elsewhere across the country, including major developments at Battersea Power Station, Embassy Gardens, New Covent Garden Market, New Wembley, Bishopsgate Goods Yard, Wood Wharf, Shell Centre, Woodberry Down, Chelsea Barracks, Aylesbury Estate and Ruskin Square. I have degrees in social policy and town planning and a doctorate in social policy and administration.
- 1.4 I am a professional member of the Royal Institution of Chartered Surveyors and a professional member of the Royal Town Planning Institute. I am a RICS Registered Valuer. I specialise in the provision of appraisal and valuation advice in respect of residential and commercial development, with a particular focus on planning and viability.
- 1.5 I and my team are responsible for the delivery of appraisal and viability advice to local authorities, developers and landowners in connection with secured lending and viability assessments relating to section 106 Agreements. I have advised over seventy local authorities on Community Infrastructure Levy charging schedules and approaches to planning obligations.
- 1.6 I have provided expert valuation evidence at numerous planning inquiries, examinations in public and informal hearings. I was recently appointed as a single joint expert by Historic England, Tendring District Council and City & Country to advise on valuation matters relating to enabling development at St Osyth's Priory. I appeared as expert witness on viability at the Westferry Printworks Inquiry in August 2019; the Sandown Racecourse Inquiry in November 2020; and at the London Fire Brigade Headquarters call-in Inquiry in December 2020. I have also provided expert reports

on secured lending valuations undertaken by other valuers, as well as expert determinations relating to valuation matters.

- 1.7 I was a member of the advisory panel drafting the Local Housing Delivery Group 'Viability Testing Local Plans: Advice for practitioners' (June 2012). I am a member of the 'Developer Contributions Technical Expert Panel' established by the Department for Communities and Local Government to advise on the use of viability assessments in local plans and development management. This panel advised on the viability section of the 2019 Planning Practice Guidance.

### **Declaration and Statement of Truth**

- 1.8 I confirm that I have made clear which facts and matters referred to in this report are within my knowledge and which are not. Those that are within my knowledge I confirm to be true. The opinions I have expressed represent my true and complete professional opinions on the matters to which they refer.
- 1.9 I confirm that I am not instructed under any conditional or success-based fee arrangement.
- 1.10 I confirm that my report complies with the requirements of RICS – Royal Institution of Chartered Surveyors, as set down in the RICS practice statement 'Surveyors acting as expert witnesses'.

## 2 Scope of evidence

- 2.1 On 11 April 2019, Wayview Limited<sup>1</sup> ('the Appellant') submitted an application to London Borough of Tower Hamlets ('the Council') for: "*Demolition of existing building and erection of a building of seven storeys, inclusive of two set back floors, plus a lower ground floor to provide 109 rooms for short-term hostel and HMO accommodation*" ('the Appeal Scheme').
- 2.2 On 3 December 2019, the Applicant submitted a Financial Viability Assessment ('FVA') prepared by Rapleys on the Appellant's behalf. The FVA reported that the Appeal Scheme would generate a residual land value of £1.12 million if 35% of units were provided as affordable. If the affordable housing were reduced to 0%, the FVA reported that the residual land value would increase marginally to £1.71 million. However, the FVA reported that the Site's benchmark land value was £8 million, so the Appeal Scheme would generate a deficit of £6.29 million (assuming no affordable housing was provided) to £6.88 million (assuming 35% affordable housing was provided).
- 2.3 The Committee report notes that modest difference in deficit and also notes that officers considered information in the FVA to be inaccurate. Officers also raised questions as to the deliverability of the scheme in the context of the deficit identified in the FVA. Applicants are required to demonstrate that their schemes are deliverable by both the Mayor of London's Supplementary Planning Guidance on viability<sup>2</sup> and the Council's Supplementary Planning Document on viability<sup>3</sup>.
- 2.4 On 18 March 2020, the Council refused planning permission on seven grounds. Reason for refusal 1 notes that "*the proposal fails to provide [an] affordable housing contribution*" and that the proposed development would be contrary to policies S.H1 (meeting housing needs), D.H2 (affordable housing and housing mix), D.H7 (housing with shared facilities) of the Tower Hamlets Local Plan 2031 (2020).

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<sup>1</sup> A wholly owned subsidiary of Interland Group Limited. The Appeal Scheme is submitted in the name of 'Rooms and Studios Management Limited' which is another subsidiary of Interland Group. Interland Group's Director's report for the year ending 31 March 2020 notes that "*it is our aim to expand our portfolio organically with 2-4 purchases annually, as well as intensification of existing assets through density maximisation*".

<sup>2</sup> 'Homes for Londoners: Affordable Housing and Viability Supplementary Planning Guidance 2017' – see paragraph 3.10 – '*Applicants should demonstrate that their proposal is deliverable and that their approach to viability is realistic. As such appraisals would normally be expected to indicate that the scheme does not generate a deficit, and that the target profit and benchmark land value can be achieved with the level of planning obligations provided. If an appraisal shows a deficit position the applicant should demonstrate how the scheme is deliverable*'.

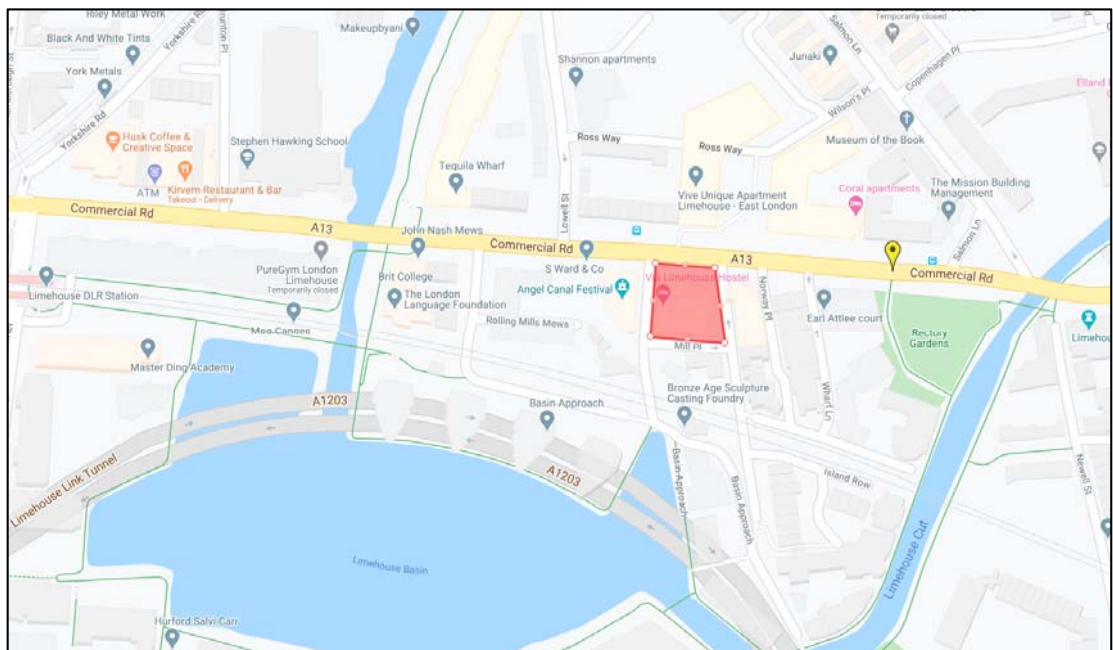
<sup>3</sup> LBTH 'Development Viability Supplementary Planning Document, October 2017' – see paragraph KR12 and KR13 – '*An applicant should demonstrate how their proposed scheme is deliverable, taking into account their proposed level of planning obligations*'.

- 2.5** My evidence considers the financial viability of the Appeal Scheme and its ability to comply with the requirements of Local Plan policies S.H1, D.H2 and D.H7.

## 3 The Appeal Site and the Appeal Scheme

- 3.1 The Appeal Site extends to 0.09 hectares and is located on the south side of Commercial Road. It is bound by Mill Place to the west and south and Island Row to the east. The Site is located close to Limehouse Basin and 0.2 miles to Limehouse Station (Docklands Light Railway and C2C services, with typical journey times of 5 minutes to Fenchurch Street Station and 6 minutes to Bank Station). The Appeal Site's Public Transport Accessibility Level ('PTAL') is 5/6a, where 6b is the highest level of accessibility.

**Figure 3.1: Location plan**



- 3.2 The existing building has three storeys on Commercial Road and Mill Place, falling to a single storey at the rear and two storeys on Island Row. The existing hostel has 52 bedrooms which are configured to provide accommodation for 263 people in a range of dormitory-style rooms.
- 3.3 The Appeal Scheme seeks an increase from 52 to 109 rooms, to be configured as 25 hostel rooms and 84 HMO rooms. The hostel would accommodate 41 people and the HMO rooms would accommodate 144 people. The replacement building would be seven storeys in height with the top two storeys stepped back. The gross internal area of the Appeal Scheme is 4,556 square metres.
- 3.4 A summary of the accommodation schedule is provided in Table 3.4.1 and a full accommodation schedule is attached as Appendix 1. It is my understanding, based

on the plans submitted with the application, that all the proposed hostel and HMO rooms will have ensuite bathrooms.

**Table 3.4.1: Accommodation schedule summary**

Hostel	Rooms	NIA (square metres)	Occupants
Single rooms	9	139.00	9
Double rooms	12	229.50	24
Accessible rooms	4	109.00	8
<b>Totals</b>	<b>25</b>	<b>477.50</b>	<b>41</b>

HMO	Rooms	NIA (square metres)	Occupants
Single rooms	24	369.90	24
Double rooms	51	1,006.90	102
Accessible rooms	9	210.50	18
<b>Totals</b>	<b>84</b>	<b>1,587.30</b>	<b>144</b>

3.5 In addition to the hostel and HMO rooms, the Appeal Scheme provides a gym, a cinema room and a reception on the ground and lower ground floors, as well as large common kitchens and living areas on each floor. In addition, the scheme provides a range of shared and private external amenity space in the form of balconies and terraces. The internal common areas extend to 1,834.2 square metres, as summarised in Table 3.5.1.

**Table 3.5.1: Common areas**

Floor	Square metres GIA
Lower Ground	337
Ground	316.5
First	190
Second	190.5
Third	244.5
Fourth	244.5
Fifth	155.6
Sixth	155.6
<b>Total</b>	<b>1,834.2</b>

3.6 The Appeal Scheme provides a range of external amenity spaces, some of which are shared by residents and some of which is private space for residents of the HMO units, as summarised in Table 3.6.1.



**Table 3.6.1: External amenity space**

Floor	Shared amenity space (square metres GIA)	Private amenity space (square metres (GIA)
Lower Ground	89.5	-
Ground	-	-
First	-	-
Second	14.9	-
Third	14.9	-
Fourth	14.9	-
Fifth	65.3	191.1
Sixth	-	44.2
<b>Total</b>	<b>199.5</b>	<b>235.3</b>

## 4 Planning policy requirements

### Affordable Housing Policy Requirements

- 4.1 Local Plan Policy S.H1 sets an overall target for 50% of all new homes (from all sources) to be affordable, and requires the provision of a minimum of 35% affordable housing on all applications providing 10 or more new residential units (subject to viability). Local Plan Policy D.H2 seeks a tenure split of 70% rented housing and 30% intermediate housing. Within the 70% rented element, paragraph 9.30 of the explanatory text of the Local Plan notes that 50% of habitable rooms should be provided as London Affordable Rent and the remaining 50% as Tower Hamlets Living Rent<sup>4</sup>. It goes on to note that the 30% intermediate element can include London Living Rent or other discounted market rent units, Shared Ownership and other intermediate housing for sale products.

### Distinction between low cost housing and affordable housing

- 4.2 Local Plan Policy D.H7 1c (Housing with shared facilities (houses in multiple occupation)) states that new HMOs will be supported where they can be secured as a long term addition to the supply of low cost housing, or otherwise provides an appropriate amount of affordable housing. Paragraph 9.70 of the supporting text to Policy D.H7 notes that the Council's "*affordable housing service – using the evidence from the latest strategic housing market assessment – will assess the proposed rent levels to determine whether the development **would primarily provide housing with shared facilities for people with low incomes***". The clear aim of D.H7 is that, whether by providing a long term addition to low cost housing or by making an appropriate contribution to conventional affordable housing, HMOs contribute to meeting the LPA's acute affordable housing needs.
- 4.3 There are thus two ways in which a developer can satisfy the requirements of Policy DH.7 1(c), either by providing housing which can be secured as a long term addition to the supply of low cost housing or, where that is not possible or is not part of the proposal, by making a policy compliant contribution to self-contained affordable housing. As Council officers have explained, although 'low cost housing' is a type of affordable housing in this context, the terms 'low cost housing' and 'affordable housing' clearly have different meanings. 'Low cost housing' is expressly defined as housing which is aimed at 'people with low incomes' and is considered to mean rents

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<sup>4</sup> Current London Affordable Rent for a one bed unit is £693 per calendar month and £857 for a Tower Hamlets Living Rent one bed unit.

that are akin to London Affordable Rents<sup>5</sup> which are rent levels set by reference to persons on low incomes.

4.4 If a scheme fails to meet this requirement (either because the housing provision is not 'low cost housing' or because any such housing is not 'secured' by a legally enforceable mechanism), then a developer can still satisfy DH.7 1(c) by making an appropriate contribution of conventional self-contained affordable housing in line with the Council's affordable housing policies.<sup>6</sup>

4.5 By reference to Policy DH.7 1 (c) it is my understanding that the Council considers that the Appeal Scheme:

(a) fails to provide low cost housing because the proposed rent levels are aimed at those on middle rather than low incomes;

(b) in any event, even if the housing provided satisfied the requirement for low cost rents (which is not accepted) in the absence of a legal obligation securing the low cost rent levels over the long term, there is nothing to prevent the Appellant or any subsequent operator increasing those rent levels in future. Therefore, the scheme does not 'secure a long term addition' to the supply of low costs housing; and

(c) on the Appellant's own case, its Scheme makes no contribution to affordable housing despite it being viable to provide such housing (for the reasons set out below).

4.6 Even if the Applicant's proposed rent levels satisfied the requirement for provision of 'low cost housing' (which they do not), in the absence of an obligation securing them as such, the Council could not have any confidence that the rents the Appellant actually intends to charge will be "*supplying a significant quantum of low cost housing*" or indeed any affordable housing, as the Rapleys FVA suggests at paragraph 10.9. Furthermore, it is likely that the Appellant actually envisages or is planning for significantly higher rents (either at the outset or over a period of time) in order to mitigate the apparent deficit reported in the statements by Rapleys and Mr Brown.

### **Application of Affordable Housing policies to HMO scheme**

4.7 Accommodating traditional affordable housing (ie self-contained C3 units) in a co-

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<sup>5</sup> As an illustration of the differences between rent levels, a one bed London Affordable Rent is currently £693 per calendar month and a one bed London Living Rent is £1,118 per calendar month.

<sup>6</sup> Policy DH.7 supporting text para. 9.69 makes clear "*Applications should seek to address housing need, as outlined in Policies S.H1 (see paragraph 9.21) and D.H2.*"

Living or HMO scheme may present practical difficulties. I am advised by officers that where such difficulties arise a payment in lieu would be an acceptable means of satisfying the requirements of Policy DH.7 1c. This is consistent with Intend to Publish London Plan Policy H16 A (9) which requires that shared living developments contribute towards traditional affordable housing and that they do so through a payment in lieu<sup>7</sup>.

- 4.8 Policies S.H1 and D.H7 apply to the HMO element of the Appeal Scheme only and not to the hostel rooms, as these are treated as sui generis use.
- 4.9 Co-Living and HMO schemes are a relatively new concept and conducting a financial viability assessment and applying affordable housing policies that were written primarily with self-contained build for sale and build for rent housing in mind is a relatively novel exercise. However, what is absolutely clear is that the Council's recently adopted Local Plan policy for HMOs policy DH.7 expects such schemes to contribute to affordable housing needs. The policy expects applicants to undertake, where relevant, a viability assessment adopting an appropriate methodology in line with development plan policy.
- 4.10 In this case, applying the established policy framework to the Appeal Scheme, the Local Plan requires a minimum provision of 35% affordable housing. Based on the rooms for shared living provided within the Appellant's HMO I have assumed in my appraisal that the Council's policies would hypothetically require that 29 of the 84 HMO units to be provided on-site as affordable, whilst recognising that in practical terms a payment in lieu is likely to be required to overcome the practical difficulties of providing conventional C3 affordable units within an HMO scheme. Testing the viability of on-site affordable housing will assist in calculating the amount of payment in lieu that would be required to satisfy the requirements of Policy D.H7 (c).
- 4.11 I note at paragraph 10.8 of their FVA, Rapleys indicate that the rents that the Appellant advised them to apply in their appraisal for the HMO units (£1,000 and £1,083 per calendar month for single and double rooms respectively) are slightly lower than London Living Rents ('LLR')<sup>8</sup> (which they suggest are £1,076 per calendar month for

<sup>7</sup> Either as an upfront payment in lieu or as an in perpetuity annual payment. Paragraph 4.16.7 of the supporting text to London Plan Policy H16 notes that "*this form of accommodation is required to contribute to affordable housing. However, because it does not meet minimum housing space standards it is not considered suitable as a form of affordable housing itself. Therefore, a financial contribution is required for affordable housing provided through the borough's affordable housing programme*".

<sup>8</sup> London Living Rent is described by paragraph 4.6.4 of the London Plan as an intermediate housing product aimed at people on medium incomes and would therefore be incorporated into the 30% intermediate housing in the 70%/30% tenure split sought by LBTH Local Plan Policy DH.2.

one bed units in 2019/20)<sup>9</sup>. The London Living Rent for 2020/21 has increased to £1,118 per calendar month.

- 4.12 The Appellant takes the London Living Rent as its benchmark for contending that its scheme is providing 'low cost housing'. However, London Living Rents are expressly aimed at people on medium incomes and are not considered by the Council to meet the requirements of Policy DH.7 1c for low cost housing. Moreover, it is important to note that the London Living Rent applies for a self-contained one bedroom unit and that there is not an equivalent London Living rent for shared living units. Generally speaking, and all other factors remaining equal, rent levels for a room in shared living accommodation will generally be lower because facilities such as kitchens are shared. There will, of course, be exceptions (for example, if there are other facilities that would not normally be available in a building of self-contained flats). These differences in rent levels are acknowledged by the supporting text to Policy H16 in the London Plan<sup>10</sup>.

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<sup>9</sup> It is unclear where this figure of £1,076 originates, as the 'London Living Rent ward benchmark data 2019/20' on the Mayor of London's website shows a monthly rent of £1,090 per calendar month for Limehouse Ward.

<sup>10</sup> Paragraph 4.16.9 of the supporting text notes that "*the rental cost of this form of accommodation is not directly comparable to the rental costs of conventional Use Class C3 housing, as shared living units are significantly smaller than the minimum housing space standard i.e. a one person dwelling of 37 sqm*".

## 5 My approach to testing the viability of the Appeal Scheme

- 5.1 I have appraised the Appeal Scheme using Argus Developer ('Argus'). Argus is a development appraisal software package which is widely used by surveying practices, developers, landowners and others involved in development appraisal. It has been used widely by both our firm and the Council's other viability framework advisors to assess the viability of development proposals in Tower Hamlets.
- 5.2 Argus Developer can be set up in two main ways. The first is to set up an appraisal to generate a residual land value, where the costs of development are entered (including a target level of profit) and deducted from the end value of the scheme to arrive at a 'residual' amount that can be used to acquire the land. The second approach is to enter a notional land cost to determine the profit generated by a scheme as an output. Rapleys adopted the former approach in their FVA and I have adopted the same approach.
- 5.3 The residual land value generated by Argus needs to be compared to a benchmark land value ('BLV') reflecting the existing use value of the Appeal Site, in accordance with paragraph 014 of the Planning Practice Guidance. The Appellant has provided a valuation of the existing hostel which is agreed to be £5.89 million, which I have agreed as set out in the Viability Statement of Common Ground. The Appellant's approach to establishing the Site's Benchmark Land Value complies with the requirements of the Planning Practice Guidance.

## 6 Appeal Scheme appraisal inputs

6.1 In this section, I review and comment on the appraisal assumptions applied by Rapleys in their FVA and (where different) inputs adopted by James Brown. It has been possible to reach agreement on some of the appraisal inputs and these are noted in the Viability Statement of Common Ground and summarised below:

- Purchaser's costs (where relevant): 5% of GDV;
- Professional fees: 8% of build costs;
- Sales agent fees (where relevant): 1% of GDV;
- SDLT: at prevailing rates;
- Profit: 15% of GDV;
- Benchmark Land Value based on the value of the existing hostel: £5.89 million;
- Mayoral CIL: Applied at prevailing rates having regard to existing floorspace and Social Housing Relief;
- London Borough of Tower Hamlets CIL: Applied at prevailing rates having regard to existing floorspace and Social Housing Relief;
- Development programme: 4 months pre-construction and 24 months construction period.

### **Gross Development Value – value of hostel rooms**

6.2 Rapley's FVA indicates that they have applied rents for the hostel and HMO rooms as follows (all rents are shown per calendar month):

- Single room: £1,000;
- Double room: £1,083;
- Accessible room: £1,100.

6.3 In his assessment, it is my understanding that Mr Brown adopts the same rents.

6.4 Rapleys acknowledge at Section 9 that these rents are not based on their own research on comparable evidence: *"We have taken advice from Interland [the Appellant] regarding the Gross Rental Income to apply to the proposed scheme"*. Rapleys have not undertaken their own independent research to validate these rents. Mr Brown does not appear to comment on an appropriate rent level at all in Section 10 of his June 2020 report and he does not indicate what rent he assumed in arriving at his capital value of £223,771 per unit at paragraph 10.10. In his September 2020 report, he again does not state what rent he considers reasonable, nor does he refer to any comparable evidence to support a particular opinion, but he does note on page

13 that “*in my opinion, the hostel room rates assumed for single rooms are too low per person*” and cites room rates from a Travelodge at Coriander Avenue E14 2AA which start at £50.99 per night excluding breakfast, which equates to a monthly rate of £1,551.

- 6.5 The rent levels adopted by the Appellant are significantly lower than the rates advertised for the single and double rooms advertised for the current hostel, which are attached as Appendix 2 and summarised in Table 6.5.1.

**Table 6.5.1: Via Limehouse Hostel existing rates**

Type of bedspace	Floor area square metres	Average nightly rate per room	Average monthly rate per room (lowest)	Total annual income per room
Twin room (exclusive use)	11	£79.20	£2,108	£25,295
Double room (exclusive use)	11	£84.60	£2,256	£26,766

- 6.6 Mr Brown has reduced the expected income from the hostel rooms on the basis of his suggestion that people would be expected to share rooms with people they did not know. Whilst this may be the case for twin rooms, this is clearly not how the Appellant intends for the double rooms to be operated in the existing hostel, as only one bed is provided, as can be seen in the descriptions and photographs of the existing hostel at Appendix 2. Furthermore, the plans submitted by the Appellant for the replacement hostel rooms also only show one bed in the double rooms, not two twin beds.
- 6.7 For some inexplicable reason, Mr Brown considers that the double rooms and the accessible rooms in the new hostel would be for shared use (i.e. by two strangers) and consequently he applies a discounted rate of £20 per person per night, discounting the revenue by £5 per room per night from the £45 per night he suggests for single rooms. Furthermore, he describes them as “twin” rooms, whereas they are clearly shown on the architect’s schedule and the submitted plans as double rooms. The same issue arises in Mr Brown’s description of the accessible rooms. Notwithstanding these issues, there is also a clear error in Mr Brown’s calculations on page 14 of his September 2020 report. His calculation of the income generated by the 12 “twin” rooms (as he incorrectly describes them) is £20 per night x 24 people (i.e. two per room) x 365 days = £131,400. However, £20 x 24 x 365 days equals £175,200, not £131,400 as he suggests. On the basis of his own rates, this error amounts to an understatement of GDV of circa £0.77 million.



- 6.8 In addition to the arithmetic error above, it is also necessary to make corrections to address Mr Brown's incorrect assumption that a discount should be applied because the double and accessible rooms will be shared by strangers; they will not be. This would increase the income by £5 per room per night, increasing the total income from the hostel rooms from £381,425 to £410,625. These corrections are summarised in tables 6.8.1 to 6.8.3.

**Table 6.8.1: Mr Brown's hotel income calculations - uncorrected**

Room type	No of rooms	JB rate	nightly	Annual income per room	Annual income
Single hostel	9		£45	£16,425	£147,825
Twin hostel	12		£40	£14,600	£131,400
Accessible hostel	4		£40	£14,600	£58,400
<b>Hostel totals</b>	<b>25</b>				<b>£337,625</b>

**Table 6.8.2: Mr Brown's hotel income calculations – 'twin' room error corrected**

Room type	No of rooms	JB rate	nightly	Annual income per room	Annual income
Single hostel	9		£45	£16,425	£147,825
Twin hostel	12		£40	£14,600	£175,200
Accessible hostel	4		£40	£14,600	£58,400
<b>Hostel totals</b>	<b>25</b>				<b>£381,425</b>

**Table 6.8.3: Mr Brown's hotel income calculations – 'twin' room and room rate errors corrected**

Room type	No of rooms	JB rate	nightly	Annual income per room	Annual income
Single hostel	9		£45	£16,425	£147,825
Double hostel	12		£45		£197,100
Accessible hostel	4		£45		£65,700
<b>Hostel totals</b>	<b>25</b>				<b>£410,625</b>

- 6.9 It is unclear why Mr Brown has applied a significant discount to rooms in the new hostel in comparison to budget hotels which are located in areas less well served by public transport in comparison to the Appeal Site. The Travelodge that he relies upon in Coriander Avenue is located 0.3 miles from East India DLR Station which only provides DLR services with typical journey times to Tower Gateway of 15 minutes. In contrast, the Appeal Site is a slightly shorter distance to Limehouse Station which provides access to both DLR (journey times of 4-5 minutes to Tower Gateway and Bank) and C2C services to Fenchurch Street (journey times of 5 minutes).

Furthermore, the Appeal Site is only 1.9 miles from Tower Gateway, whereas the Docklands Travelodge is located 3.8 miles, making the Appeal Site more attractive for those wishing to cycle or walk to central London instead of using public transport.

- 6.10 I have therefore applied a rate of £51 per room per night, which reflects the advertised rate for the Travelodge Docklands, but note that this could be higher, given the Appeal Site's superior location. In addition, the Appeal Scheme provides on-site facilities that are not available at Travelodge Docklands, including a cinema room, large common areas, kitchens and a gym. There are no material reasons why the rates charged in a hostel providing private rooms with en-suites would be any lower than rates charged by budget hotels for comparable accommodation. My calculations of total income are summarised in Table 6.10.1.

**Table 6.10.1: Hostel income**

Room type	No of rooms	Nightly rate	Annual income per room	Annual income
Single room	9	£45	£16,425	£147,825
Double room	12	£51	£18,615	£223,380
Accessible double	4	£51	£18,615	£74,460
<b>Hostel totals</b>	<b>25</b>			<b>£445,665</b>

- 6.11 After deducting the same 25% of the gross income to cover operating costs as applied by Rapleys and Mr Brown, the net income amounts to £334,249. I have applied the same investment yield of 4.25% to the net income as adopted by Rapleys and Mr Brown, generating a capital value of £7,864,676.
- 6.12 Mr Brown has indicated that the Appellant is prepared to provide a planning obligation which would limit the occupancy of the new hostel rooms to one person in a single room and two people in a double room. This would have no material impact on the income generated as neither Mr Brown nor I have assumed that the rooms could accommodate higher numbers of occupants.

### **Gross Development Value – HMO rooms**

- 6.13 As previously noted, Rapleys have relied upon “*advice*” from the Appellant on the rates to be applied to the HMO rooms in the Appeal Scheme and no independent evidence of potential room rates is provided.
- 6.14 The closest Co-Living scheme is The Collective's scheme at Canary Wharf which offers flexible occupancy, ranging from one night to long term stays. Nightly rates are

£98.90 for a 16 square metre standard room, while monthly rates for a standard room start at £1,300. Other co-living schemes offer long term rents at similar levels, including Gravity Co-Living (Camden) at £1,646 per calendar month; and Mason & Fifth (Bermondsey) at £1,400 per calendar month (see Appendix 3).

- 6.15 Rapleys have applied the same rates for the HMO rooms as the hostel rooms, which significantly understates the potential income. Whilst the rents for shared accommodation applied by Rapleys are comparable to the LLR which is a sub-market intermediate rent level targeted at those on medium incomes, (although they do not satisfy the Local Plan policy DH.7 1c definition of ‘low cost housing’), but in the absence of a Section 106 obligation securing them as such, they cannot be considered to meet Local Plan policy requirements.
- 6.16 In the absence of any planning obligation controlling or securing the Appellant’s affordable (albeit not low cost) rents, I have applied market rents to the HMO rooms which reflect the location of the Appeal Scheme; the amenities provided; and the features of the rooms, all of which appear to have been over-looked by Rapleys and Mr Brown. In particular, the rooms on the fifth and sixth floors have access to extensive private open space, including terraces which extend to as much as 26.8 square metres, yet the rent applied by Rapleys and Mr Brown for these rooms is identical to the rent for rooms on lower floors with no external private open space.
- 6.17 A schedule of the rents I have applied is attached as Appendix 4. The average annual and monthly income is summarised in Table 6.17.1.

**Table 6.17.1: HMO rooms average annual and monthly income**

Room type	No of rooms	Average annual income	Average monthly income
Single en-suite	24	£13,458.09	£1,121.51
Double en-suite	51	£14,610.40	£1,217.53
Accessible double en-suite	9	£14,349.50	£1,195.79

- 6.18 Rapleys apply the same capitalisation rate to the HMO rooms that they adopt for the Hostel rooms. CBRE’s valuation specialists indicate that capitalisation rates for HMO rooms “sit between the build to rent and PBSA [purpose built student accommodation] sector for long stay income, depending on location, design and tenant profile”, while “yields on short stay income would be higher than for long stay and more aligned to hotel cap rates” (See Appendix 5). For Build to Rent schemes in Transport for London Zone 2, CBRE advise capitalisation rates of 3.25%. I have applied this capitalisation

rate in my assessment, reflecting the rents I have assumed being aimed at long term occupancy (e.g. 6 month or similar length tenancy) rather than short term stays (e.g. periods of a few days or weeks), making the accommodation more akin to build to rent housing in terms of investment yield.

- 6.19 The HMO rooms generate a capital value of £27,629,310, assuming all rooms are let at market rents. In contrast, Mr Brown's GDV for the HMO rooms is £18,796,764, reflecting the rent levels advised by the Appellant.
- 6.20 In his September 2020 statement, Mr Brown relies heavily upon capital values of co-living schemes agreed in viability assessments and there is little consideration of the gross and net income that the Appeal Scheme units will generate. Given that improving net income from its site appears to be the Appellant's principal objective in bringing forward its scheme (see Rapleys report paragraph 14.3), rather than achieving a value through an onward sale, Mr Brown's approach is unreliable.
- 6.21 Furthermore, it is unclear to me why Mr Brown considers a co-living scheme in Croydon to be comparable to a scheme in Limehouse, given the relative distances of each to central London.

### **Food and beverage revenue**

- 6.22 Although I am advised by Mr Brown that the Appellant does not intend to provide a central catering facility<sup>11</sup>, I note that the model adopted in other budget hotels is for the provision of 'breakfast boxes' or similar meals prepared off-site and sold on an on-demand basis. Travelodge Docklands sell their breakfast boxes for £5.25 per meal. Applying the same model at the Appeal Scheme and assuming a conservative 50% take-up of this offering, gross income would amount to £40,000 per annum. In addition, vending machines selling drinks and confectionary are likely to generate revenue in the order of £15,000 per annum. Assuming an EBITDA of 35% on this income, the profit would be around £19,000 per annum.
- 6.23 I have applied a 4.25% investment yield to the EBITDA resulting in a capital value of £450,000.
- 6.24 It is unclear from the planning submission how the cinema room and gym are to be operated and whether these will generate any revenue. I have assumed that they will

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<sup>11</sup> This is unusual for shared living schemes/Co-Living schemes as it is my understanding that both of the Collective schemes at Old Oak Common and Canary Wharf provide on-site cafes.

not at this stage but reserve my position pending further investigation. If these facilities are separately charged, this revenue should be reflected in the appraisal. Conversely, if these facilities are not separately charged for, then this should be reflected in the rents charged and it does not appear that Rapleys nor Mr Brown have done so.

### **Build costs**

6.25 The Appellant's cost plan has been prepared by 3-Sphere. RLF have reviewed the Appellant's cost plan on the Council's behalf. The Statement of Common Ground dated 24 November 2020 indicates that the respective costs advised by the two cost consultants are as follows:

- RLF: £13,400,401 (£2,945 per square metre);
- 3-Sphere: £14,252,284 (£3,132 per square metre).

6.26 There is a difference of £851,883 between the cost consultants. I have relied upon RLF's cost in my appraisal, but the difference in costs is not material to my conclusion that, all other inputs remaining equal, this scheme can make a substantial policy compliant contribution to affordable housing. RLF's total cost is inclusive of demolition and contingency and I have not shown these separately in my appraisal.

6.27 It is my understanding that the main differences between RLF and 3-Sphere are in relation to the following:

- Design risk and contingencies;
- Services;
- Space heating and cooling;
- Electrical installations Siteworks; and
- Contractor's overheads and profit.

The reasons for those differences are set out in statement prepared by RLF.

### **Finance rate**

6.28 Both Rapleys and Mr Brown incorporate finance at 7% which is higher than rates I have recently seen in viability appraisals for student housing and similar rented housing developments. I have applied a finance rate of 6% in my appraisals.

6.29 I also note that in reality, the Appellant will not need to finance the acquisition of the

Site, as it is already in their ownership. Below I set out my conclusions which appraise the scheme on objective standardised basis and separately taking into account the reality that there is no land purchase in the context of the scheme.

### **Profit, purchaser's costs and sales agent fees**

- 6.30 I note that both Rapleys and James Brown have incorporated deductions in their appraisals for purchaser's costs (£1,341,574) and sales agent's / sales legal fees (£369,899). Although these rates are in line with normal appraisal metrics, I note that the Appellant is developing the Scheme itself in order to improve the gross to net income relationship. In reality, the Appellant will not incur these costs as it will be holding the completed Appeal Scheme within its portfolio. Although viability assessments are carried out on an 'applicant neutral' basis with standardised inputs, the reality of the situation is that the Appellant will not incur these costs and they could arguably, be removed from the calculation. I consider the impact this has when discussing my appraisals in the next section.
- 6.31 The same issue applies to profit. Profit in a residual appraisal is intended to reflect the risk associated with the speculative development and sale of a new asset. Profit is typically applied at a rate of 15% of GDV on build to rent housing on the basis that the completed units will need to be sold to an operator. The Appeal Scheme is clearly different, as the current owner (the Appellant) is bringing the development forward and they will retain the completed building. There is no speculation in the normal sense of a developer needing to sell the housing being constructed. Clearly there will be the risk of letting the units once available for occupation, but this risk is implicit in the investment yield applied to the rental income. However, we are guided by the PPG to use standardised inputs and treat viability appraisals in an 'applicant neutral' manner.
- 6.32 That said, Mr Brown states in his June 2020 report that "*an Applicant has a right to take a view (without prejudice) as to whether they are willing and able to progress a development based upon a certain lower than normal level of profit*". On his own numbers, the Appeal Scheme generates a loss, so the Applicant is presumably prepared to proceed on the basis of a zero profit, which is logical given that Rapleys have indicated at paragraph 14.3 of their report that the Appellant is motivated by improving their gross to net rental returns; their focus is on income generation and not achieving a profit from a sale. Arguably, it is therefore inappropriate to reflect a profit in the appraisal at all.

- 6.33 Neither Rapleys nor Mr Brown have applied premiums to the EUV which is consistent with their argument that the Appellant is redeveloping the hostel to improve the gross to net rental returns, rather than seeking to maximise returns from an onward sale of the facility. I agree that, in the circumstances, applying a premium to the EUV would be inappropriate.

## 7 Development appraisals

- 7.1 I have undertaken my own development appraisals based on the inputs discussed in the preceding section. As noted in Section 4, officers have advised that the Appellant's proposed rent levels are not considered to be 'low cost rented housing' for the purposes of Policy DH.7 1 (c) and therefore traditional affordable housing should be provided (most practicably) through a payment in lieu. In order to test the capacity of the Appeal Scheme to meet the requirements of Local Plan policies S.H1 and D.H7, I have tested a number of rent levels which would satisfy the requirements in terms of overall level of provision and tenure. In doing so, it is important to note that co-living units do not fit within the normal classification of housing that the Council seeks and there is not an equivalent affordable rent type specific to Co-living/HMO schemes. To address this issue, I have applied discounts to market rents which would satisfy the requirements of policies S.H1 and D.H7 so that I can calculate a payment in lieu.
- 7.2 By way of a comparison to rent levels for 'traditional' affordable housing tenures (which makes up 70% of the affordable housing requirement of Policy S.H1), and recognising that the co-living product in question is not the same, one bed rents for self-contained units (per calendar month) are as follows:
- London Living Rent: £1,118;
  - Tower Hamlets Living Rent: £857;
  - London Affordable Rent: £693
- 7.3 Table 7.2.1 summarises the scenarios I have tested and the rentals applied to individual units are attached as Appendix 6. As a proxy for the rents likely to be charged for hypothetical on-site affordable rented units (i.e. the 70% of affordable housing sought by Policy S.H1) I have applied varying discounts to market rents, between 50% and 70% of market rent. It should be noted that a rent of 50% of market rent is most likely to reflect the rents that would be sought by Policy SH.1. For the remaining affordable housing units (the 30% intermediate housing element sought by Policy S.H1), I have applied a discount of 20% to market rent, reflecting the minimum discount required in the definition of affordable housing in Appendix 2 of the NPPF. As noted previously, the Applicant's proposed rents are also slightly lower than market rents, and could in principle be regarded as 'affordable' (although not sufficiently low to satisfy the requirements of Policy DH.7 1c for 'low cost housing') but only if they are secured as such by a planning obligation. My understanding is that the Appellant



is resisting entering into such a planning obligation for any of the units, which leaves the rents completely unconstrained. It is therefore likely that, in practice, the Appellant will charge rents which are significantly higher and this would be consistent with their objective of improving net income generated by the Scheme. Any subsequent operator would be free to charge whatever rents it liked. This flexibility would address the substantial deficit that both Rapleys and Mr Brown's appraisals have identified.

**Table 7.2.1: Rents applied in the appraisals (applied to 70% of the affordable units, with the remaining 30% levied at 80% of market rents)**

Percentage discount to market rent	Average Rent per calendar month	Average Rent per annum
30%	£818	£9,818
40%	£701	£8,415
50%	£584	£7,013

- 7.4 As noted in Table 7.2.1, for the purposes of my appraisals, I have applied rent levels to 35% of the units which are discounted below market rents. All of these rent levels are capable of satisfying Local Plan policies S.H1, D.H2 and D.H7 as they are lower than the equivalent rent for one bed properties let at London Living Rents, Tower Hamlets Living Rents or London Affordable Rent.
- 7.5 The results of my appraisals incorporating 35% affordable housing (assuming that for 70% of the affordable units discounts to market rents of 30%, 40% and 50% are applied; and for the remaining 30% of 'intermediate' affordable units, a discount to market rent of 20% is applied) are summarised in Table 7.5.1. In all cases, these residual land values should be compared to the Appellant's Benchmark Land Value of £5,890,000 to determine whether the scheme (with a given level of affordable housing provision) is viable.

**Table 7.5.1: Appraisal results – 35% affordable housing**

Affordable housing (% of discount to market rent)	Residual land value	Appellant's benchmark land value	Surplus
30%	£8,236,690	£5,890,000	£2,346,690
40%	£7,829,905		£1,939,905
50%	£7,423,119		£1,533,119

- 7.6 I have also considered the results reflecting the circumstances of the Appeal Scheme, recognising there is unlikely to be no onward sale of the completed hostel and HMO units, and removing purchaser's costs, sales agents fees and profit, as outlined in paragraphs 6.28 to 6.30. The results of my appraisals incorporating 35% affordable housing, assuming the same discounts to market rents are applied as outlined in paragraph 7.3) summarised in Table 7.6.1.

**Table 7.6.1: Appraisal results – 35% affordable housing (reflecting no onward sale with profit, purchaser's costs and sales agent fees removed)**

Affordable housing (% of discount to market rent)	Residual land value	Appellant's benchmark land value	Surplus
30%	£14,541,056	£5,890,000	£8,651,056
40%	£14,011,722		£8,121,722
50%	£13,482,389		£7,592,389

- 7.7 As noted previously, it is unlikely that the Council would wish to secure on-site affordable housing and the Council's preference would be to secure a payment in lieu to fund provision of affordable housing on other sites in the borough. I have calculated a payment in lieu by comparing the residual land value generated by a scheme let at full market rents, to a scheme incorporating 35% affordable housing provision, assuming rents at a 50% discount to market rent.
- 7.8 As noted in Table 7.4.1, the scheme incorporating 35% affordable housing (with 70% of the units let at rents at a 50% discount to market rent and 30% let at rents at a 20% discount to market rent) would generate a residual land value of £7,423,119. If the rents for all the units are set at 100% of market rent, the residual land value would increase to £9,818,978 (see Appendix 10).
- 7.9 The payment in lieu is therefore £9,818,978 minus £7,423,119, equalling £2,395,859.

## 8 Conclusions

- 8.1 The assessments undertaken by Rapley and Mr Brown result in significant deficits against the value of the existing Hostel. Rapleys argue at paragraph 14.3 of their report that the Appellant is motivated by improving their gross to net rental returns, while Mr Brown seeks to explain away the apparent deficit by suggesting that “*an applicant has a right to take a view (without prejudice) as to whether they are willing and able to progress a development based upon a certain lower than normal level of profit*”. On the base appraisal that he is presenting, that profit is actually a loss of £1.3 million.
- 8.2 There is a degree of common ground on the inputs to be used in the appraisals. The two main disputed matters are the build costs, where there is a difference between the parties of £851,883; and the value of the completed hostel and HMO rooms. It is my opinion, as set out in Section 6 of my evidence, that Mr Brown has significantly understated the value generated by the completed development.
- 8.3 The rents used by the Appellant’s viability advisors are slightly lower than London Living Rent for one bed units. While recognising that the proposed HMO units in the Appeal Scheme are not a like-for-like housing product and acknowledging the real differences between the two (which are likely to mean lower rent levels for shared living schemes), London Living Rent is in principle an affordable housing tenure that is acceptable under the Council’s Local Plan Policy S.H1. However, LLR is an intermediate rent which would not satisfy the requirement under the first limb of Policy DH.7 1(c) to provide low cost housing for those on low incomes. In any event, the rooms at these rents are not secured as affordable by a planning obligation.
- 8.4 My appraisals indicate that the Appeal Scheme can viably provide a range of affordable options, with 35% of units let at rents that are discounted by up to 50% from market rent. All of the potential levels of rental income I have tested generate residual land values that exceed the £5.89 million benchmark land value, including a rent that would be broadly equivalent to London Affordable Rent.
- 8.5 Furthermore, I have also drawn attention to costs that will not – in reality – be borne by the Appellant relating to the disposal of the completed development to a third party. Owning an operating rented housing is one of the Appellant’s core businesses and there is unlikely to be a disposal, given the stated objectives of improving the overall net income generating capacity of the Scheme. The theoretical costs of disposals

and profit to reflect speculative development could in theory be removed from the appraisal, resulting in a significant improvement in the residual land values generated. However, even without discounting those costs the Appeal Scheme would still be capable of making a substantial, policy compliant contribution towards affordable housing.

- 8.6 In light of my assessment, I conclude that there are no reasonable grounds for the Appeal Scheme failing to provide 35% affordable housing with a tenure mix that complies with the requirements of Policy D.H2. Still less is it justified for the Appellant to argue that its scheme can provide zero affordable housing.
- 8.7 It is unlikely that the Council would, in practice, seek on-site affordable housing in a shared living scheme and a payment in lieu would be sought instead. My calculation of a payment in lieu based on the uplift in residual value arising from not providing any affordable housing on site equates to £2.40 million.