



East Riding Of Yorkshire Council

Affordable Housing Viability Assessment
Analysis of increasing S106/CIL Contributions &
the potential impact of Affordable Rent Tenures



St Pauls House
23 Park Square South
Leeds
LS1 2ND

July 2012

1. Introduction

Following the completion of the Affordable Housing Viability Assessment (the Assessment) for East Riding of Yorkshire Council (ERYC) in March 2010, ERYC have reappointed DTZ to look at a number of elements in more detail, providing further analysis and additional information to assist in formulating policy.

The original Assessment helped ERYC to understand the impact of affordable housing provision on development viability. The findings highlighted that the requirement for affordable housing impacted on development viabilities, particularly in the current financial climate. In addition, DTZ have completed an addendum to the Assessment which considered the potential role for offsite contributions, the threshold for delivering affordable housing and also examined the Goole housing market area in greater detail. In response to changes to national planning policy and consultation responses on the Core Strategy Further Consultation, further questions have emerged which this addendum now considers:

1. If ERYC were to incorporate a £3,000 per unit allowance for Community Infrastructure Levy (CIL) instead of the current S106 contributions allowance of £2,000 in the original Assessment, what impact would this have on development viability?
2. What impact might the introduction of Affordable Rent tenure have on development viability across the East Riding of Yorkshire.

The purpose of this addendum report is to consider these questions in turn.

The Original Affordable Housing Viability Assessment (AHVA) Study Approach

At the core of the AHVA study approach is a detailed viability modelling exercise. This examines the impact on viability of different affordable housing contributions on hypothetical development schemes in different parts of the study area. It has therefore been necessary to develop a typology of different sites that are likely to come forward for housing development across the East Riding area and to test the viability of these hypothetical sites under a set of different development scenarios.

The original AHVA tests a number of development scenarios as follows:



Baseline: This scenario related to the market which was prevalent at the time of the commission modelling (December 2009). This reflected one of the lowest market positions of recent times and the level of viability was demonstrated to be low.

Height of the Market: This scenario replicated the market conditions at the height of the last property cycle in 2007.

A range of other scenarios were tested between these two extremes in order to consider a range of market scenarios which may occur across the life time of the policy. These are outlined below. For details of individual scenario assumptions please refer to the main AHVA report.

1. Base position with increased build rates – this is the most likely scenario to affect the market at the out turn of the recession
2. Base position with increased and decreased revenues – staged % changes in revenues
3. Base position with increased and decreased build costs – staged % changes in costs
4. Base position with no additional contribution for other S106 elements

The remainder of this report considers each of the questions identified following the assessment in turn as follows:

Chapter Two: CIL Impact

Chapter Three: The potential Impact of Affordable Rent on Development Viability



2. Community Infrastructure Levy Impact

Since the completion of the original Affordable Housing Viability Assessment (AHVA), ERYC have resolved to implement the Community Infrastructure Levy. The Council wish to understand whether the Core Strategy Further Consultation Policy HBHM2: Meeting the need for affordable housing is flexible enough to allow for some level of CIL requirements once work on the CIL charging schedule has been completed.

The Core Strategy Further Consultation Policy HBHM2: Meeting the need for affordable housing proposes that in order to meet the East Riding's affordable housing need, developments of 10 housing units or more in the Major Haltemprice Settlements, Principal Towns and Local Service Centres and 3 housing units or more elsewhere, will be required to provide affordable housing. The figure in the Draft Policy sets out the following Affordable Housing Requirements by Housing Market Area:

Beverley	25% Requirement
Bridlington	20% Requirement
Holderness	15% Requirement
Hull Borders	25% Requirement
Wolds	25% Requirement
Howden	25% Requirement
SARM	20% Requirement
Goole North & South	5% Requirement

It is these draft thresholds and requirements which will be tested as part of this additional analysis.

The original AHVA study, made an allowance of £2,000 per unit for additional S106 items over and above an affordable housing requirement. The recommendations of the AHVA were used to inform the affordable housing policy in the Core Strategy Further Consultation, Responses to the consultation suggested that the policy requirements were not flexible enough to allow CIL to be charged on housing development. This addendum tests the requirements set in the Further Consultation considering the ability of the schemes to deliver further additional payments. It was decided to replace the £2,000 per unit S106 charge with £3,000 per unit to see whether this increase substantially effects viability.

In order to test the impact of inflating contributions to a level of £3,000 per unit, the original EVA models were rerun and the viability levels tested. Each of the housing market areas was

tested in turn with the Goole Housing market further segregated into its sub market areas in accordance with the AHVA Addendum. The impact of increasing these contributions on each of the market areas is considered in turn below but the summary position of results is as follows.

Market Area	Percentage Affordable Housing Tested	Height of the market		Baseline		Overall	
		Sites that became unviable (traffic light changed to red)	Change in IRR	Sites that became unviable (traffic light changed to red)	Change in IRR	Sites that became unviable (traffic light changed to red)	Change in IRR
Beverley	25%	6% - 2 sites	0.5-0.9%	0% - 0 sites	0.5-0.9%	6% - 2 sites	0.5-0.9%
Bridlington	20%	0% - 0 sites	0.5-0.8%	0% - 0 sites	0.5-0.8%	0% - 0 sites	0.5-0.8%
Holderness	15%	3% - 1 site	0.6-0.8%	0% - 0 sites	0.5-1.5%	3% - 1 site	0.5-1.5%
Hull borders	25%	3% - 1 sites	0.5-0.8%	0% - 0 sites	0.5-0.9%	3% - 1 sites	0.5-0.9%
Wolds	25%	3% - 1 site	0.5-0.9%	0% - 0 sites	0.6-1.4%	3% - 1 site	0.5-1.4%
Howden	25%	0% - 0 sites	0.5-0.7%	0% - 0 sites	0.5-0.9%	0% - 0 sites	0.5-0.9%
SARM	20%	0% - 0 sites	0.5-0.6%	0% - 0 sites	0.5-0.8%	0% - 0 sites	0.5-0.5%
Goole N and S	0%	25% - 9 sites	0.5-0.7%	0% - 0 sites	0.2-0.7%	25% - 9 sites	0.2-0.7%

2.1 Individual Market Areas Results

Beverley

At the baseline position modelling showed that Internal Rates of Return (IRR's) decreased by between 0.5% and 0.9% and no traffic light colours changed when S106 contributions were increased from £2,000 per unit to a CIL scenario of £3,000 per unit. There was no change in the overall viability of sites at the baseline.

At the height of the market only 6% of sites (2 sites) became unviable when the S106/CIL requirement was increased from £2,000 to £3,000 and this only occurred when high



percentages of social rented product were introduced. The IRR for each site decreased between 0.5% and 0.9%.

The slight change in viability at the height of the market is not significant and would not alter the recommendations of the original AHVA. A 25% target in the Beverley housing market is justified, when considering the assumptions/analysis and circumstances used within the original AHVA and the scenarios tested.

Bridlington

At the baseline position modelling showed that Internal Rates of Return (IRR's) decreased by between 0.5% and 0.8% and no traffic light colours changed when S106 contributions were increased from £2,000 per unit to a CIL scenario of £3,000 per unit. There was no change in the overall viability of sites at the baseline.

At the height of the market position, No variance is seen in the overall viability when contributions are increased from £2,000 per unit to £3,000 per unit. The IRR for each site decreased by between 0.5% and 0.8% for the height of the market scenario when contributions were raised from £2,000 per unit to £3,000 per unit.

Therefore, as no change in viability occurred across the scenarios tested, the recommendations of the original AHVA would not alter had £3,000 per unit been incorporated within the modelling.

Holderness

At the baseline position, IRR's decreased by between 0.5% and 1.5% for the baseline scenario and no traffic light colours changed between the two scenarios therefore not impacting upon the overall viability.

At the height of the market only 3% of sites (1 site) became unviable when the S106/CIL requirement was increased from £2,000 to £3,000 and this only occurred when high percentages of social rented product were introduced. The IRR for each site decreased between 0.6% and 0.8%.

The slight change in viability at the height of the market is not significant and would not alter the recommendations of the original AHVA. A 15% target in the Holderness housing market is



justified, when considering the assumptions/analysis and circumstances used within the original AHVA and the scenarios tested.

Hull Borders

At the baseline position, modelling showed that Internal Rates of Return (IRR's) decreased by between 0.5% and 0.9% and no traffic light colours changed between the £2,000 and £3,000 S106/CIL scenarios. There was no change in the viability of sites at the baseline.

At the height of the market only 3% of sites (1 site) became unviable when the S106/CIL requirement was increased from £2,000 to £3,000 in any of the scenarios tested. The IRR for each site decreased between 0.5% and 0.8%.

The slight change in viability at the height of the market is not significant and would not alter the recommendations of the original AHVA. A 25% target in the Hull Borders housing market is justified, when considering the assumptions/analysis and circumstances used within the original AHVA and the scenarios tested.

Wolds

At the baseline position, modelling showed that Internal Rates of Return (IRR's) decreased by between 0.6% and 1.4% and no traffic light colours changed between the £2,000 and £3,000 S106/CIL scenarios. There was no change in the viability of sites at the baseline.

At the height of the market only 3% of sites (1 site) became unviable when the S106/CIL requirement was increased from £2,000 to £3,000 in any of the scenarios tested. The IRR for each site decreased between 0.5% and 0.9%.

The slight change in viability at the height of the market is not significant and would not alter the recommendations of the original AHVA. A 25% target in the Wolds housing market is justified, when considering the assumptions/analysis and circumstances used within the original AHVA and the scenarios tested.

Howden

At the baseline position, IRRs decreased between 0.5% and 0.9%. No variance is seen in the overall viability when contributions are increased from £2,000 per unit to £3,000 per unit.



The IRR's decreased by between 0.5% and 0.7% for the height of the market scenario when contributions were raised from £2,000 per unit to £3,000 per unit. No variance was seen in this market area at the height of the market position when Section 106 contributions of £2,000 were replaced with CIL values of £3,000. As no change in overall viability was seen the recommendations of the Addendum AHVA remain unaltered.

SARM

At the baseline position no variance is seen in the overall viability when contributions are increased from £2,000 per unit to £3,000 per unit. The IRR's decreased by between 0.5% and 0.8% for the baseline scenario when contributions were raised from £2,000 per unit to £3,000 per unit.

At the height of the market position, no variance was seen in this market area at the height of the market position when Section 106 contributions of £2,000 were replaced with CIL values of £3,000. The IRR's decreased by between 0.5% and 0.6% for the height of the market scenario when contributions were raised from £2,000 per unit to £3,000 per unit. As no change in overall viability was seen the recommendations of the Addendum AHVA remain unaltered.

Goole North and South

At the baseline no viability was seen with either £2,000 or £3,000 CIL/S106. At the height of the market scenario, nine sites (25%) saw amber lights change to red lights when the CIL/S106 contributions was increased. This shows a weakness of these housing markets and their ability to deliver any residential accommodation.

At the baseline IRRs decreased from 0.2% to 0.7%. At the height of the market IRR's decreased by between 0.5% and 0.7% when contributions were raised from £2,000 per unit to £3,000 per unit.



2.2 Threshold Analysis

The original AHVA tested a site threshold of 15 units and went on to complete some additional analysis as to tipping points for different areas. However, the production of the Issues and Options Core Strategy document identified a number of options for setting affordable housing site size thresholds and therefore DTZ were appointed to undertake the Addendum AHVA to assess these options and this section of the report should be read alongside this document.

In order to test the impact of increasing S106/CIL on the thresholds outlined in The Core Strategy Further Consultation Policy HBHM2: Meeting the need for affordable housing analysis of site thresholds by area has been undertaken. The bespoke models for each of the areas have been updated to include an assessment of schemes where the threshold for affordable housing is 3, 5 and 10 units and these sites were then tested at contributions of £2,000 and £3,000 per unit to assess viability. The Draft Core Strategy Policy H2 suggests differing threshold requirement for Urban and Rural areas and as such this has been assessed both in the AHVA Addendum and this report.

The results of the modelling work mirrored that highlighted above and again concluded that it was clear in this scenario that very little variance was seen and no material impact would be had on the conclusions of the original AHVA or Addendum Report by increasing these additional contributions by £1,000 per unit.

2.3 Conclusion

In conclusion, this additional modelling informs us that the impact of raising contributions by £1,000 per unit is such that it will not materially alter the conclusions and recommendations reached in the original AHVA or the addendum report, and therefore the thresholds and requirements in the draft policy are supported. In most of the circumstances tested the variance in viability was less than 1%. The Core Strategy Further Consultation Policy HBHM2: Meeting the need for affordable housing is drafted in a way that would enable further higher charges of CIL to be considered alongside the economic viability of individual schemes through the submission of an economic viability assessment. Should the CIL charging schedule be produced to require a higher contribution than £3,000 per unit, the affordable housing requirement stated in Figure 1 of Policy HBHM2 can be negotiated with ERYC should this prove to have a detrimental effect on development viability.



3. Affordable Rent

The second part of his additional brief relates to consideration of what impact might the introduction of Affordable Rent tenure have on development viability across the East Riding of Yorkshire? In order to answer the question we must first consider the background to this tenure type and why it has been introduced by the Government. The supply of housing has not kept up with demand in recent years for a variety of reasons and there is a requirement for additional homes generally and affordable homes in particular. There are an estimated 4.5 million people on housing waiting lists across the UK, many of whom have no realistic chance of being allocated a home and are locked out of the private housing market due to the constraints on mortgages, requirement for substantial deposits and unaffordable prices. The problem is exacerbated by the cuts in public spending which are impacting on the availability of grant funding to deliver affordable homes.

In autumn 2010, the Government announced a new housing tenure - Affordable Rent. Affordable Rent is to be made available for the 2011 – 2015 Affordable Homes Programme and is intended to provide Registered Providers greater flexibility in the rents and tenancy terms that they could offer in order to help deliver up to 150,000 new affordable homes.

On the 9th December 2010, following the Spending Review, the Minister for Housing and Local Government, The Rt Hon Grant Shapps announced further details of the new Affordable Rent model to be offered by Registered Providers. Shapps stated that the new Affordable Rent tenure had been designed to increase the delivery of new affordable homes by making the best possible use of existing housing stock, new homes and constrained public subsidy, to provide a diverse offer for the range of people who need to access affordable housing through providing alternatives to traditional social rent.

Affordable Rent will offer Registered Providers the flexibility to convert vacant, social rented or new build properties to Affordable Rented properties (at a rental level of up to 80% of market rent) in certain circumstances. Registered Providers will be able to convert empty properties to the new Affordable Rent tenure when they have reached an agreement with the Homes and Communities Agency (HCA) about how the additional income will be reinvested to deliver new affordable housing. It is envisaged that Affordable Rent properties will be allocated in the same way as social rent properties.

The new Affordable Rent tenure falls within the definition of affordable housing following an amendment to PPS3:Housing and therefore Section 68 of the Housing and Regeneration Act 2008 applies. National Policy was further updated through the publication of the National

Planning Policy Framework on 27 March 2012 where Affordable Rent is incorporated within the definition of Affordable Housing provided in Annex 2: Glossary which states that *Affordable Rented housing is let by local authorities or private registered providers of social housing to households who are eligible for social rented housing*. Affordable Rent will continue to be subject to rent controls by the HCA that will require no more than 80% of the local market rent (including service charges, where applicable) to be charged for this tenure type.

The Impact of Affordable Rent on Development Viability

Affordable Rent was introduced by the Government in recognition that there will be much less money available in the way of grants to support affordable housing development. By enabling Registered Providers to charge more rent, it is hoped Registered Providers will be able to source more private sector funding. The Affordable Rent model allows Registered Providers to charge up to 80% of gross market rents in contrast to circa 50% of market rent currently achievable for a Social Rented unit. Therefore, as income streams are increased, units which have a higher rental stream will provide greater revenue to the Registered Provider allowing them to source higher levels of funding. This will allow them to borrow more and purchase the property at a higher value from a Developer and thus aid development viability. It is important to recognise that the impact of the introduction of affordable rent on development viability is not proven to date.

Conclusions on the impact of Affordable Rent on development viability and the results of the AHVA study in particular, can only be reached once the extent to which these units are delivered by Registered Providers and ERYC is known. To-date, no Affordable Rent S106 units have been delivered within the East Riding of Yorkshire. This picture is not uncommon across the Yorkshire and Humber Region where the delivery of Affordable Rented units on new build schemes has been low. Given the presumed higher income generated by the Affordable Rent product, it is likely developers would seek to deliver more of this product as opposed to social rent.

The traditional model of affordable housing delivery in East Riding of Yorkshire is for completed units to be sold to a Registered Provider by the Private Developer at a negotiated discount below Market Value. The affordable revenue adopted in the AHVA study reflects this process, and is expressed as a proportion of market value sales revenues. Each site is different, but for the purposes of the AHVA modelling, hypothetical values of 35% of Market Value for Social Rented homes and 65% of Market Value for Intermediate homes have been adopted. If Affordable Rent tenure is introduced it may be that the overall revenue from affordable housing may increase above these values due to the increased revenue streams.



However there is currently insufficient evidence both locally and nationally to reach conclusions as to the value of Affordable Rent units expressed as a percentage of Market Value.

It is felt that the introduction of Affordable Rent tenures will have the highest impact in high value areas of the East Riding (such as Beverley). In areas where property prices and rental values are low (such as Goole) there will be very little difference between Market Rent and Social Rent and therefore little to be gained in viability terms from the introduction of Affordable Rent. In areas of higher rental values, the ability of a Registered Provider to charge 80% of market rent would result in significantly increased revenues which will feed through into higher capital values.

It should be noted that under the Affordable Homes Programme new homes are to be charged at whichever is the higher of Affordable Rent or Formula Rent. Therefore, the introduction of Affordable Rent will not negatively impact upon development viability.

The delivery of Affordable Rent across the East Riding of Yorkshire remains uncertain and untested. It is unclear what level of delivery, will be seen. Therefore, it is difficult to determine what impact Affordable Rent will have on development viability. Affordable Rent tenure has only been incorporated in the 2011-2015 Affordable Homes Programme with, as yet, no indication of extension past this date. Consequently ERYC must ensure flexibility with regard to delivering this tenure type (if sought by Registered Providers on new developments). The impact of its delivery on the provision of affordable housing provision through the Core Strategy policy cannot be proven, however it is unlikely to have a detrimental impact and in some cases may improve the viability of development.