
Appeal Decision

Hearing held on 7 October 2015

Site visit made on 7 October 2015

by Ava Wood DipARCH MRTPI

an Inspector appointed by the Secretary of State for Communities and Local Government

Decision date: 2 November 2015

Appeal Ref: APP/K5030/S/15/3087233

Sugar Quay, Lower Thames Street, London EC3R 6EA

- The appeal is made under Section 106BC of the Town and Country Planning Act 1990 against a failure to determine that a planning obligation should be modified.
 - The appeal is made by Sugar Quay Holdings Limited against the City of London Council.
 - The development to which the planning obligation relates is demolition of existing building and construction of a new building of basement, ground, part 9, part 11 storeys comprising 165 residential units and 658 sqm of retail/café and restaurant use at ground floor.
 - The planning obligation, dated 16 September 2013, was made between the Mayor and Commonalty and Citizens of the City of London, the Wardens and Commonalty of the Mystery of Fishmongers of the City of London and Sugar Quay Guernsey Limited.
 - The application Ref: DHS/0487 is dated 5 March 2015.
 - The application sought to have the planning obligation modified by replacing the definition of the Affordable Housing Contribution to fix the amount payable at the specified sum of £11,203,000 with indexation to be added.
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Decision

1. The appeal is dismissed. The planning obligation, dated 16 September 2013, made between the Mayor and Commonalty and Citizens of the City of London, the Wardens and Commonalty of the Mystery of Fishmongers of the City of London and Sugar Quay Guernsey Limited shall continue to have effect.

Procedural Matter

2. Following the end of the hearing the parties agreed a form of wording to be used in the decision, should I be minded to allow the appeal. A revised Proposed Modified S106 was also submitted within the timeframe agreed. The additional material forms Document 18.

Main Issues

3. These are: whether the proposed development is economically viable, if it remains subject to the affordable housing obligation as it currently exists; and if not, what modification to the obligation is needed for the development to be made viable.

Reasons

Preliminary and Agreed Matters

4. Before turning to matters relating to the financial viability of the scheme, it is worth recording a number of relevant facts and key matters agreed.

- The appeal site is located on the northern waterfront of the River Thames, adjacent to Tower Pier and to the west of the Tower of London.
- Planning permission was granted on the site in June 2011 for demolition and construction of an eight storey office building with retail use at ground floor.
- The scheme to which this appeal relates proposes residential accommodation on the first to sixth floor of about 23,000 sqft per floor, tapering down to a minimum of 10,549 sqft from seventh to the tenth floors. Duplex penthouse accommodation is proposed from the seventh floor upwards.
- The planning obligation related to the permission provides for an Affordable Housing Contribution of £15,006,816 (indexed) in lieu of on-site provision.
- The first instalment of £7,503,408 (indexed) is to be paid to the Corporation on or before the implementation date. The second instalment of the same amount is also to be paid prior to the implementation date. Four months before the implementation date the developer is obliged to either confirm the second instalment amount or submit a revised viability assessment identifying the proposed amount of the second instalment.
- The applicant (Sugar Quay Guernsey Limited)¹ submitted an updated viability assessment in February 2014 to demonstrate that the development could not afford to make any additional affordable housing payment beyond the first instalment.
- Following a disagreement on valuation with the Corporation's advisers (Gerald Eve), and by mutual consent, an independent expert was appointed. Mr Leahy of Bespoke Property Consultants (BPC) determined in January 2015 that the amount of the second instalment due (as at July 2014) is £3,699,592. This would produce a total Affordable Housing Contribution of £11,203,000.
- SQGL accepted the findings of BPC and the application for modifying the planning obligation was made on that basis.
- In February 2015 the Planning and Transportation Committee resolved not to accept the expert's findings, despite the chief planning officer and development director's recommendation to do so. The Corporation's decision to continue to press for the full payment of £15,006,816 gave rise to the application under s106BA and this appeal.
- The appellant is proposing modification of the s106 to replace the definition of the Affordable Housing Contribution by fixing the total amount payable at the sum of £11,203,000. The total figure represents the first instalment sum of £7,503,408 together with the amount of £3,699,592 identified by BPC as the second instalment. The Affordable Housing Contribution is to be paid in full on or before the implementation date.

The Scheme's Viability

5. In establishing the extent to which the development could bear the costs of the affordable housing provision, a number of viability exercises have been carried out on behalf of the Council and the appellant. The parties' appraisals are

¹ The development and s106BA applications were submitted in the name of Sugar Quay Guernsey Ltd (SQGL). SQGL transferred its ownership interest into a separate company (Sugar Quay Holdings Ltd) and the applicant name was amended during the application process.

based on an agreed benchmark site value of £60m and a return on cost of 20%. BPC's findings were governed by these same agreed values. A number of other input values were agreed, including car parking income and ground rents on the revenue side of the equation, with fees, marketing and sales on the development costs side. While there is some disparity in the cost of construction, the differences are not significant or determinant.

6. The main areas of dispute arising from the parties' respective positions, and on which this decision now focuses, can be narrowed down to the following three headings:
 - Relevant valuation date.
 - Gross development value for the residential element of the scheme.
 - Gross development value for the commercial element of the scheme.

Relevant Valuation Date

7. The appellant maintains that the economic viability of a development, in the context of an application under s106BA and subsequent appeal under s106BC is to be "...assessed by reference to market conditions, costs and other relevant factors as they are at the date of the application."² In other words, March 2015. A number of factors are said to point to that position, which is regarded as consistent with the provisions under s106BA and s106BC while also reflecting the DCLG guidance³. It is also said that the indications in the guidance do not point to two different valuations – i.e. at the application and the appeal stages. The Council's case, on the other hand, is that "*viability must be judged in market conditions current at the time of the determination.*"⁴
8. I note, and the parties agreed at the hearing, that valuation date is not fixed by either the Town and Country Planning Act or any other statute. While paragraph 7 of the DCLG guidance suggests that the viability evidence supporting the application should be submitted with the appeal, it also goes on to state that the "*...test for viability is that the evidence indicates that the current cost of building out the entire site (at today's prices) is at a level that would enable the developer to sell all the market units on the site (in today's market) at a rate of build out evidenced by the developer, and make a competitive return to a willing developer and a willing landowner.*" The developer is expected to demonstrate that the affordable housing obligation as currently agreed makes the scheme unviable under current market conditions. The revised appraisal is also expected to be based on current market conditions. The guide further advises that "*...clear, appropriate and up to date evidence is to be submitted.*" The language used repeatedly in the guidance (today's market, current market conditions and up to date evidence, for instance) points to the economic conditions relevant to the present time. In other words, to take account of current or up to date circumstances.
9. Using a valuation date at the time of consideration of the appeal may not be suitable for all cases under s106BA or s106BC. However, given the narrow margins separating the parties' respective positions in this specific case, the most up to date information available on key variables provides a better understanding of the ability of the development scheme to deliver on its affordable housing obligations. The validity of this approach is borne out by

² Document 3 – Appellant's written submissions in relation to relevant valuation date

³ Section 106 affordable housing requirements – Review and appeal, April 2013

⁴ Document 4 – Council's written response to Document 3

the March, May, July and October summary appraisals, which demonstrate that even minor fluctuations impact on the economics of the development. Adopting a valuation date as close to the determination date as possible also has the advantage of taking account of the effects of recent notable events. The outcome of the general election or implications of the stamp duty land tax (SDLT) changes for instance, which the parties evidenced as factors relevant to the value and sale of residential properties in London.

10. The evidence from both parties covers a period between March and October 2015. In the interest of consistency of approach and, because it helps to understand the parties' respective predictions of revenue and costs between those dates, my reasoning below refers to the March as well as October appraisals.

Residential Sales Values

11. The appellant's valuations comprise updates of the BPC mid-point pricing appraisal (the Base Appraisal). BPC adopted a valuation date of July 2014 and relied on the residential sales values provided by selling agents based in the City. The Council and SQGL had agreed to the appointment of Hurford Salvi Carr (HSC) to advise on pricing as part of the independent expert's determination. The appellant's March and October 2015 updates, prepared by DS2, used data on cost inflation from Gleed's Quarterly Inflation report and Savills Prime Central London Index for apartments.
12. The Council's approach to establishing sales values is based on a market report undertaken by Hamptons International – a residential estate agent with an office in the City of London. The report derives its pricing of the Sugar Quay apartments from nine potentially comparable schemes, of which five were also considered by HSC.
13. The DS2 update results in an average sales value of £1,835 per sqft (March 2015), against Hamptons' expectation of £1,916 per sqft. The equivalent sales values for October 2015 are £1,881 and £1,916 respectively.
14. The indexing method used by DS2 raises some concerns. First, it relies on a pricing base set in July 2014. Second, the Savills Prime Central London Index is based on second hand sales and does not take account of new-build premiums. While I understand that indices in second hand properties may be the norm, the use of indexing to establish the value of new-build properties in a location that BPC referred to as having worldwide appeal raises questions about the robustness of such an approach.
15. On the other hand, I agree that valuing the Sugar Quay apartments against likely comparables is difficult, given the paucity of directly comparable developments and locations. The absence of similar properties in this location caused the appellant to refer to the site as 'risky and unestablished'. The site is indeed unique for the position it occupies on the edge of the City with south facing river views. Although views to the north towards an office block are less appealing, the BPC report described this as a world class location. It may not benefit from the range of cultural facilities and variety of eating establishments enjoyed by properties on the South Bank. Sugar Quay nonetheless is in a prime position, adjacent to a world heritage site and with good access to facilities and transport choices.

16. At the hearing the appellant painted a less than optimistic picture for the sale of Sugar Quay apartments at the prices estimated by Hamptons. The prime reasons being:
- competition from other developments along the riverfront, especially on the South Bank;
 - the foreign investment market is slimmer now and asking prices are reducing as a result;
 - the market for high-end properties has come under pressure since introduction of the SDLT in the Chancellor's 2014 Autumn Statement, other Government initiatives have raised 'offshore vehicle' difficulties and the market is slowing in the wake of the mortgage market review.
 - less off-plan sales due to the volatility of the market.
17. The difficulties in selling the bigger and more expensive units at The Heron development were held up as examples of the situation which could befall the sale of the Sugar Quay penthouse suites. Indeed, the largest disparity between the parties lies in the estimated values of the high-end units. This fact was recognised in the BPC report. The appellant also does not agree with Hamptons' 25% premium on river fronting units.
18. Taken in the round, my opinion is that Hamptons' pricing conclusions are to be preferred for the following reasons:
- The pricing derives from a professional consideration of indicative achievable values on a unit by unit basis, as opposed to a more broad brush approach of applying indices across the board.
 - The pricing is informed by the asking prices across a range of recent developments around the City and on the South Bank, albeit strict parallels are non-existent. That The Heron sales took place some time ago, partly explains the reason for Hamptons' exclusion of those properties from their considerations.
 - The comparables are not too different from those selected by HSC. Five out of the nine analysed by Hamptons were also used by HSC.
 - The Council may not have agreed with the outcome of the BPC determination, but the HSC asking average prices in December 2014 are not too dissimilar to Hamptons' achievable values. Indeed, the individual appraisals prepared by DS2 (March, May, July and October) show rates per sqft which are not all that different from Hamptons' values.
 - The values estimated for the river view units are lower than those commanded at the nearest comparable at 1 Tower Bridge on the South Bank. The units in this development are valued at an average of some £2,613.
 - Although Savills' pricing is based on 50% of units with no river views, Hamptons have adopted a more conservative figure of 70%, which provides some comfort with regard to the robustness of their evidence.
 - The river view uplift is not applied across the board but on a unit by unit basis.
19. The appellant is critical of the Hamptons' report for a number of reasons. Notably for selection of inappropriate comparables and because the pricing of

the developments considered is higher when compared to EGi values. The views expressed above cover those points.

20. The appellant also draws attention to the evidence from land registry which shows that the number of properties of £2m and above accounts for only 5% of City of London transactions in the 12 months to mid-2015. By contrast, Hamptons work on the basis of a significantly higher proportion of Sugar Quay units priced at £2m and above. The land registry evidence perhaps demonstrates a shortage of high-end properties in the City and a reason to be optimistic about pricing due to lack of supply. But, even the DS2 appraisals are based on 23 units priced at £4m and above (3 beds and penthouses) and 60 of the 2 beds units at just below £2m (£1,837,448 in March and £1,883,921 in October). In other words, the appellant's evidence is also based on near enough 50% of units selling for close to £2m or above.
21. Although the appellant fears that the untried nature of the location raises the risk profile of the development, the developers have described it as "*...an unparalleled position. It is a landmark in design, in location and in London's continuing story.*" The uniqueness of the location and design quality of the scheme could also set a new benchmark. The penthouses face south with river views, and a large number of the smaller units at lower floors are also orientated to the south. The evidence shows that the 2012 SDLT increases were absorbed by the markets. The latest increases are more substantial but its effects could potentially be neutralised by reduction in uncertainties in the sale of high-end properties since the general election. In my judgement, having regard to all of the evidence before me, I conclude that there are reasonable prospects of achieving the values estimated by Hamptons.
22. To conclude, for the reasons explained above, Hamptons' average per sqft figure of £1,916 is a realistic basis for establishing the gross development value of the scheme.

Commercial Values

23. The difference between the parties is attributed to yield: 5.5% (Council) as against 6% (appellant). I note that the BPC report assumes a yield of 6% on the commercial elements of the scheme. This was justified on the basis that the scheme's café location would be separated from the main Tower of London offer and its size would be large against other opportunities. The Council considers that attracting a Michelin star restaurant and the restaurant's location justifies the lower yield.
24. While I am more inclined to agree with the reasoning for the higher yield, both parties agree that the level of disparity is small and not significant enough to unduly affect the economics of the scheme.

Other Matters and Conclusion on Viability

25. The Council's sales velocity evidence is not accepted by the appellant, and indeed the appraisals are based on agreed sales rates. However, Hamptons' evidence shows that better rates might be achievable with the scheme selling well to both the domestic and international markets.
26. I agree that, for the purposes of the appeal, viability analysis should be carried out on a current basis and not by reference to potential growth, particularly as there are contrary views on the rate of growth in both residential values as well as build cost inflation. However, the appellant's own figures show that between March and October 2015 the increase in gross development value

- exceeds costs to the extent that the affordable housing contribution payable also increases from £10,081,696 to £12,105,706.
27. The upward trend goes some way to reduce the already narrow margin between the parties. It also reveals the extent to which small variations in inputs can achieve incremental but beneficial outcomes, such as increased contribution towards affordable housing.
28. The appellant confirmed that the developer would proceed with a return on costs of 19.3% (the return estimated in March 2015 with an affordable contribution of just over £11.2m). There is no similar assurance that the residential scheme would proceed with a profit return of 17.1% or 18.3% (appellant's predictions of return with the £15m affordable housing contribution at March and October 2015 prices respectively) but, as confirmed at the hearing, the decision is for the board to make at the appropriate time.
29. I have read the appeal decisions referred to in the Council's evidence. However, the circumstances vary to the extent that the matters at issue addressed in those appeals are not directly applicable to the case before me. As noted in the appellant's submissions, the valuation date issue did not arise in the other appeal cases.
30. The GLA letter of March 2015 expresses satisfaction with the conclusions of the expert determination, goes on to acknowledge that the dispute may continue and accepts that there may be merit in reviewing prices achieved. The letter neither supports nor opposes either party's position.
31. Given my conclusions on the likely prospect of achieving the Council's estimated values for the residential units, it follows that the development permitted is a viable proposition with the current affordable housing obligation in place. The scale of reduction in value from applying the 6% yield is unlikely to alter that position. Overall, my conclusion is that the scheme is capable of bearing the cost of the Affordable Housing Contribution offered by the current obligation. There is no need therefore to consider whether modifications to the obligation are necessary to make the project viable.
32. Having taken into account all other matters raised none carries sufficient weight to alter the balance of my considerations or decision to dismiss the appeal.

Ava Wood

Inspector

APPEARANCES

FOR THE APPELLANT:

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|-------------------|------------------------------|
| Neil King QC | Landmark Chambers |
| Tim Simpson | CPC London |
| Pascal Levine | DS2, Development Consultants |
| Chris Beard | DP9 Limited |
| Dominic Grace | Savills |
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FOR THE LOCAL PLANNING AUTHORITY:

| | |
|--------------------|---|
| Neil Cameron QC | Landmark Chambers |
| Robert Fourt FRICS | Gerald Eve LLP |
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| Matthew Haycox | Director, Hamptons International |
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| Annie Hampson | Chief Planning Officer, City of London Corporation |
| Peter Shadbolt | Assistant Director (policy), City of London Corporation |
| Deborah Cluett | Assistant City Solicitor, City of London Corporation |

DOCUMENTS RECEIVED AFTER THE HEARING OPENED

- 1 Appellant's opening statement
- 2 City of London Corporation's opening statement
- 3 Appellant's submissions in relation to the relevant valuation date
- 4 City of London Corporation's response on valuation date
- 5 City of London Corporation's bundle of core documents
- 6 Statement of Common Ground
- 7 DS2 Development Appraisal, March 2015
- 8 DS2 Development Appraisal, July 2015
- 9 DS2 Development Appraisal, May 2015
- 10 DS2 Development Appraisal, October 2015
- 11 Summary of Gerald Eve and DS2 development appraisals
- 12 Gerald Eve Financial Evaluation Summaries, March-October 2015
- 13 Sensitivity Analysis, profit on costs
- 14 Sir John Lyon House, asking and selling prices
- 15 Letter from Mr Grace (Savills) to Mr Simpson (Candy & Candy), dated 12 February 2014, re-pricing the scheme
- 16 Extract from CBRE "London living- A borough by borough showcase", July 2015, submitted by City of London
- 17 Extract from Savills' "Spotlight – Prime London Residential Market", Autumn 2015, submitted by the appellant
- 18 Material submitted after the hearing closed