Valuation of land for affordable housing
1st edition, guidance note

The provision of affordable housing has been high on all political agendas for many years but there has been limited guidance to valuers on the methodology behind the valuation of land for that purpose.

This guidance note aims to assist the valuer in the approach to the valuation of land for affordable housing by focussing on the affordable housing element of a scheme.

Although the methodology behind the valuation of land for affordable housing has much in common with a conventional valuation of development land, it can be very complex as it relates to specialised markets. These valuations therefore require a high level of expertise.

The main topics covered are:

- What is affordable housing?
- Establishing the facts and development potential
- Methods of valuation
- The approach to a residual valuation
- The impact of subsidies
- Reporting the valuation.

This guidance has been prepared with regard to valuation practice in England and Wales.
Valuation of land for affordable housing

RICS guidance note

1st edition (GN 59/2010)
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RICS Valuation Standards (the ‘Red Book’) 

RICS (Royal institution of Chartered Surveyors) is the leading organisation of its kind in the world for professionals in property, land, construction and related environmental issues. As part of our role we help to set, maintain and regulate standards – as well as providing impartial advice to governments and policymakers.

To ensure that our members are able to provide the quality of advice and level of integrity required by the market, RICS qualifications are only awarded to individuals who meet the most rigorous requirements for both education and experience and who are prepared to maintain high standards in the public interest.

Members who qualify as valuers are entitled to use the designation ‘Chartered Valuation Surveyor’ and, in addition to compliance with the general Rules of Conduct applicable to all members, must also comply with the RICS Valuation Standards, generally referred to as the ‘Red Book’.

This guidance note describes the standard of work that is expected of a reasonable, competent valuer experienced in the subject to which this note relates.

RICS has in place a regulatory framework. Where a valuer undertakes work that has to comply with the Red Book that valuer is also required to register with RICS. Registration enables RICS to monitor compliance with the valuation standards and take appropriate action where breaches of those standards have been identified.

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Production of the guidance was also greatly assisted by the participation of a wide range of consultees and stakeholders throughout its development.
This is a guidance note. It provides advice to members of RICS on aspects of the profession. Where procedures are recommended for specific professional tasks, these are intended to embody ‘best practice’, that is, procedures which in the opinion of RICS meet a high standard of professional competence.

Members are not required to follow the advice and recommendations contained in the guidance note. They should, however, note the following points.

When an allegation of professional negligence is made against a surveyor, the court is likely to take account of the contents of any relevant guidance notes published by RICS in deciding whether or not the surveyor has acted with reasonable competence.

In the opinion of RICS, a member conforming to the practices recommended in this guidance note should have at least a partial defence to an allegation of negligence by virtue of having followed those practices. However, members have the responsibility of deciding when it is appropriate to follow the guidance. If it is followed in an inappropriate case, the member will not be exonerated merely because the recommendations were found in an RICS guidance note.

On the other hand, it does not follow that a member will be adjudged negligent if he or she has not followed the practices recommended in this guidance note. It is for each individual chartered surveyor to decide on the appropriate procedure to follow in any professional task. However, where members depart from the good practice recommended in this guidance note, they should do so only for good reason. In the event of litigation, the court may require them to explain why they decided not to adopt the recommended practice.

In addition, guidance notes are relevant to professional competence in that each surveyor should be up to date and should have informed him or herself of guidance notes within a reasonable time of their promulgation.
1 Scope

1.1 The aim of this guidance note is to assist the valuer in the approach to the valuation of affordable housing development land. It focuses on the valuation of land for the affordable housing element of a scheme.

1.2 This guidance note has application only in England and Wales.

2 Introduction

2.1 The methodology behind the valuation of land for affordable housing has much in common with a conventional valuation of development land, therefore this guidance note should be read with an understanding of the contents of VIP 12: Valuation of development land.

2.2 The valuation of affordable housing land can be very complex and relates to specialised markets. It requires a high level of expertise. Valuers are reminded that PS 1.5 (‘Knowledge and Skills’) states that they must possess the skills, knowledge and understanding to undertake the valuation competently, and recognise that assistance may be needed from other professionals.

2.3 A development scheme may range from one that is 100% social housing to one where social housing is an element of a larger mixed tenure residential or mixed use development. This guidance note gives advice only on the approach to the valuation of the land for the affordable housing element of a development scheme (the other elements being valued as discussed in VIP 12) on a cleared, or greenfield site, or where the site is to be redeveloped by removing all, or substantially all, of the existing buildings and constructing new buildings. It does not apply to redevelopment based on a refurbishment of existing buildings with limited demolition although many of the principles will apply.

2.4 Some Planning Authorities favour a distribution of the affordable housing elements, known as ‘pepperpotting’, throughout the scheme for social or other reasons. This distribution of accommodation within blocks of flats or throughout a housing or mixed use development precludes the identification of a separate land value that can be attributed specifically to the affordable housing element. Its consideration will form part of the assessment of the value of the site as a whole. However an apportionment of the value of the whole site can be made between that used for affordable and open market accommodation.

2.5 There are two approaches to the valuation of development land for affordable housing:

- comparison with the sale price of land for comparable development (see paragraph 6); or
- assessment of the value of the completed scheme and deduction of the costs of development (including developer’s profit) to arrive at the underlying land value. This is known as the residual method (see section 7).

2.6 In practice, a valuation would rely on both techniques with the comparable method being used more as a ‘reality check’. The degree to which either or both are used depends upon the nature of the development being considered, the certainty about the costs and factors that relate to affordable housing, and the complexity of the issues involved.

2.7 This guidance note has been written specifically with regard to practice in England where the provision of affordable housing is governed through the planning system. Where it differs, the practice in Wales is noted separately. In Scotland, and Northern Ireland the provision of affordable housing is governed through the housing policy and, although the means of provision may differ in detail, the valuation approach is essentially the same and this guidance note may be adapted as necessary.

3 What is affordable housing?

3.1 The key starting point is an understanding and appreciation of what is affordable housing.

3.2 In England, Planning Policy Statement 3 (PPS3) 2006 from Communities and Local Government contains a definition (at Annex B, p.25) of affordable housing:

‘Affordable Housing includes social rented and intermediate housing, provided to specified eligible households whose needs are not met by the market. Affordable housing should:

- meet the needs of eligible households including availability at a cost low enough for them to afford, determined with regard to local incomes and local house prices; and

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EFFECTIVE FROM 1 JUNE 2010"
include provision for the home to remain at an affordable price for future eligible households or, if these restrictions are lifted, for the subsidy to be recycled for alternative housing provision.'

3.3 In Wales the definition of ‘affordable housing’ is contained within Technical Advice Note 2: Planning and Affordable Housing (TAN 2).

‘This is housing provided to those whose needs are not met by the open market. Affordable housing should:

- meet the needs of eligible households, including availability at low enough cost for them to afford, determined with regard to local incomes and local house prices; and

- include provision for the home to remain affordable for future eligible households, or if a home ceases to be affordable, or staircasing to full ownership takes place, any subsidy should generally be recycled to provide replacement affordable housing.

Affordable Housing can be considered in two categories:

- Social Rented Housing – provided by local authorities and registered social landlords (RSLs) – the latter also referred to more commonly as housing associations (see below);

- Intermediate Housing – where prices or rents are above those of social rented housing but below market housing prices or rents. This can include equity sharing schemes (for example HomeBuy). Intermediate housing differs from low-cost market housing, which the Assembly Government does not consider to be affordable for the purpose of the land-use planning system.'

3.4 To identify eligible households, studies are undertaken at a local level in order to assess housing needs, as well as the relationship between incomes and house prices.

3.5 There are different tenure types that qualify as affordable housing. The following diagram shows the two main tenures and types of housing within each tenure type:

3.6 A More detailed explanation of each tenure type and affordable product is contained in Appendix A.

4 Establishing the facts

4.1 In addition to establishing the type and amount of affordable housing it is essential that the valuer has an awareness of the characteristics of the existing site and an adequate knowledge of each of the development components (see paragraph 2 of VIP 12 for a more detailed discussion on establishing the facts).

4.2 The purpose of the valuation will influence the extent of the information that is required.

5 Assessing development potential

5.1 While much of paragraph 3 of VIP 12 is applicable, and the methodology for the valuation of land for affordable housing has many aspects in common with a conventional appraisal of land for private residential development, there are important differences.

5.2 Arguably, the key differences that affect revenues and costs are:

- the impact of regulation in the affordable housing sector;
• the impact of spatial planning policies relating to an evidence base of local housing need and,
• the availability of subsidies in the form of grants or otherwise.

5.3 Whilst a conventional appraisal is not undertaken within a policy vacuum, the constraints on costs and revenue for affordable housing have a greater proportional impact upon the end site value.

Planning influences in England

5.4 The impact of national and local spatial planning policies and the delivery of well-being outcomes required in Sustainable Communities Strategies, and Local and Multi Area Agreements (LAAs/MAAs) has to be considered when undertaking a valuation of land for affordable housing.

These will be supported by a local housing strategy, local affordable housing policy, and the supporting evidence base required in PPS3, i.e. the Strategic Housing Market Assessment (SHMA), the Strategic Housing Land Availability Assessment (SHLAA) and the economic appraisal of the local affordable housing policy. Particular regard should be given to the RICS information paper entitled, Spatial planning and infrastructure delivery.

Planning influences in Wales

5.5 Housing, town and country are devolved matters and different considerations will apply:

• Local Development Plans replaced the Unitary Development Plans in 2005. There has been a transitional period to cover their introduction.
• The Wales Spatial Plan (WSP) was adopted by the Welsh Assembly Government in November 2004. This would appear to be less land use based than the regional based strategy in England. Planning and policy decision making are required to take account of WSP provisions.
• The Welsh equivalent of a PPS is a TAN. They differ in form and content.
• The Welsh Assembly is seeking powers to suspend Right to Buy in areas where there is a housing need.

Planning constraints

5.6 In a private residential appraisal, the scheme make up will be based upon permitted massing, densities, saleability and a unit mix that will generate the optimum development and highest value for a developer. When assessing development potential for affordable housing land it will be necessary to assess not only the issues above but any constraints on the type of housing, for example, dwelling size, type, price and tenure, that may be appropriate to comply with local and national policy on affordable housing and local housing need.

5.7 In England PPS3 provides for such constraints to be identified as plan-wide and overall tenure mix targets and as location or site specific requirements. The impact of these requirements will depend on the soundness of the supporting evidence base.

5.8 In Wales TAN2 will be applicable.

5.9 Additionally, 100% affordable housing schemes may not necessarily incur the same planning obligations as a private led residential scheme and consideration should therefore be given to a local authority’s relevant planning policies when assessing the value to be reported.

5.10 A valuation can be undertaken to appraise either:

• the value of land for a 100% affordable housing scheme; or
• to assess the value of a section 106 package of affordable housing units provided as a planning obligation as part of a wider development; or
• to assess the value of land required to be used for affordable housing as a planning condition.

6 Valuing by the comparison method

6.1 An explanation of valuations by the comparison method is contained in paragraph 4 of VIP 12.

6.2 The usefulness of the comparison method of valuation of land for affordable housing is limited as a consequence of the amount and complexity of legislation and the planning restrictions associated with affordable housing. This means that the form and scale (and therefore value) of permitted developments can vary widely from site to site, even within the same local authority. As a result the comparable method may only, at best, be useful as a ‘reality check’ on the valuation, and even then the valuer should be aware of the impact that the availability of grant funding can have on the value of land for affordable housing.
7 Valuing by the residual method

7.1 The methodology detailed in VIP 12 is generally applicable, but there can be more complexities in assessing Gross Development Value (GDV) and development costs in a residual appraisal for affordable housing land than for a private led scheme and these require further explanation.

7.2 There are two main components required to ascertain the value of land for affordable housing:
- assessing the potential GDV or revenue of the scheme; and
- deducting any costs associated with constructing the scheme.

8 Establishing the GDV

8.1 Whilst the value of the completed development (or GDV) for a private led residential development is relatively straightforward to calculate, often using comparables to work out private sales rates, the process of calculating the GDV for affordable housing is more complex.

8.2 There are three main components that make up the GDV of land for affordable housing:
1. Rental and capital receipts from the affordable units. Income from this source will be from either:
   - The capitalised net annual rents (for a given time period at a given discount rate) from the social rented, intermediate rent, and the rental element of the new build HomeBuy units; or
   - The capital receipts from initial equity sales and future tranche sales of new build HomeBuy, shared equity and discounted market sale units.
2. Any proceeds that may be reinvested from staircasing receipts, Right to Acquire (RTA) or external subsidies, such as Social Housing Grant (SHG).
3. Any internal registered provider of subsidy.

8.3 To reflect the many variables in a complex scheme valuers will usually adopt a discounted cash flow valuation approach.

Social rent

8.4 In England in 2001, a rent influencing regime was implemented as a result of a government Housing Green Paper in 2000 that identified marked variations in rental levels being charged by registered providers to tenants who lived in similar sized properties in similar locations. The aim was to link rents to local earnings and property values. The Housing Corporation issued guidance in 2001 entitled Rent Influencing Regime: Implementing the rent restructuring framework. The functions of the Housing Corporation were subsequently transferred to the Tenant Services Authority (TSA).

8.5 The rents that can be charged on social rent units are calculated in accordance with the guidance at levels below market rents. In order to ensure that they are affordable to those in housing need who cannot afford to access market or intermediate tenure housing, the levels vary from one region to another. The rents were indexed based on an assessment of the value of the property in January 1999. The basis of valuation adopted is EUV as set out in the RICS Valuation Standards at UKPS 1.3.

8.6 In 2002, the government required registered providers to calculate a target rent for each property so that by 2012 the actual net rent of the property would be adjusted to match this target rent (in real terms). The target rent is calculated through a formula that uses relative county earnings, relative property values and number of bedrooms to arrive at the target rent. In order to arrive at the target rent the net rent is tracked against an annual rate of RPI + 0.5% plus or minus £2 per week. Once the target rent has been reached rents track RPI movement + 0.5% per annum. The TSA issue guidance on rents, rent differentials and service charges changes from time to time and the latest guidance is available on www.tenantservicesauthority.org.

8.7 The target rents are subject to rent caps that are set according to the number of bedrooms. The rent caps are published annually by the TSA. Rent caps are essential in higher value areas in order to keep rents affordable for tenants on lower incomes. Rent caps track RPI movement + 1% per annum.

8.8 In Wales the rent is calculated from guidelines supplied by the Welsh Assembly Government.
8.9 Gross passing rents are the sum of the weekly target rents prior to deducting any costs incurred.

8.10 The net passing rent is calculated by deducting the following costs from the gross rent receivable by the registered provider:

- management costs;
- repairs & maintenance costs;
- allowance for voids & bad debts;
- annual sinking fund (including allowance for major repairs); and
- unrecoverable service charge.

8.11 In order to arrive at the GDV the aggregate of the annual net passing rents is capitalised over the period of the cashflow at an appropriate discount rate reflecting:

- the sustainability of the existing rental income;
- the likely rate of future rental growth;
- the condition of the portfolio;
- the level of outgoing required to maintain the maximum income stream;
- the likely performance of the portfolio in relation to its profile and location;
- the real cost of borrowing; and
- the long-term rate of gilts.

8.12 If it is assumed that a Right to Acquire (RTA) will occur and that net receipts will be reinvested by a registered provider, this capital should be built into the cashflow and discounted back at an appropriate rate as set out in ‘RTA and Staircasing Receipts’ below.

**Types of intermediate housing**

8.13 Intermediate tenure products are aimed at those who can afford to pay more than social rent but less than market price or market rent. The main types of intermediate tenure products are:

(a) Intermediate Rent;
(b) new build HomeBuy (formerly known as shared ownership);
(c) shared equity;
(d) discounted market sale (non HC compliant); and
(e) rent to HomeBuy (England only).

8.14 They are aimed at potential occupiers who qualify within specific income criteria that are linked to local average earnings and housing needs assessments at a local level. Some local authorities will link affordability criteria to a maximum percentage of a household’s net income that should be spent on housing costs.

**a) Intermediate Rent**

8.15 In order to calculate the GDV for the intermediate rent units the aggregate of the net annual passing rent receivable is capitalised over the period of the cashflow at an appropriate discount rate.

The passing rent of the unit is calculated as the lesser of:

- 80% of the weekly market rent of the unit; or
- the weekly rent that a tenant would be able to afford having regard to local policy on affordability and the proportion of a household’s net income that should be spent on housing costs. The income criteria for applicants will be set by individual local authorities to ensure that intermediate rent products are only accessible by those who are unable to afford open market housing.

The net passing rent is calculated by deducting the following costs from the rent receivable by the registered provider:

- management costs;
- repairs & maintenance costs;
- allowance for voids & bad debts;
- annual sinking fund (including allowance for major repairs); and
- unrecoverable service charge. This may vary considerably depending upon the accommodation and levels of service to be provided.

Thereafter, the rents can be grown in excess of RPI + 0.5% per annum, but any growth must be both affordable and fair to tenants.

**b) New build HomeBuy (England only)**

8.16 For new build HomeBuy units, the lump sum receivable from the initial equity sale is added to the capitalised rent, capitalised at an appropriate discount rate, charged on the retained equity. The HCA currently specify a minimum threshold of 25% initial equity sale and limit the rent on the retained equity (still owned by the registered provider) at a maximum of 3% of the retained security for an
individual unit or a maximum average of 2.75% across the scheme as a whole.

8.17 If it is assumed that staircasing will occur and that net receipts will be reinvested by a registered provider, this capital should be built into the cashflow and discounted back at an appropriate rate as set out in ‘RTA and Staircasing Receipts’ below.

8.18 In weaker market conditions no staircasing may occur over the first one or two years of the cash flow with the remainder of the staircasing spread over 10–15 years depending upon the amount of intermediate provided in the development. If it is a large scheme then staircasing to 100% (if permitted in the planning consent and s. 106) may take a number of years.

c) Shared equity

8.19 Shared equity products comprise an initial equity sale. A combination of the initial equity lump sum receivable and any future staircasing receipts will constitute the total GDV for the scheme as no rent is charged on the equity retained by the registered provider.

8.20 The consideration of the impact of staircasing will be the same as set out in paragraphs 8.17 and 8.18.

d) Discounted market sale (non HC compliant)

8.21 The GDV for discounted market sale will comprise the lump sum receivable from the purchaser of the unit. There is no rent chargeable on the unsold equity and no potential for future staircasing as the unit is discounted from the market value into perpetuity.

e) Rent to HomeBuy (England only)

8.22 GDV for rent to HomeBuy can be calculated on one of two bases:

Either:

On the assumption that the unit will continue to be rented in perpetuity and the occupier will never purchase the unit under the new build HomeBuy scheme. In this case the GDV is arrived at by capitalising the net rent, calculated as set out in 8.15 into perpetuity in the same way as an Intermediate Rent.

Or:

Through a combination of:

- the net rent receivable for the initial rental period (5 year maximum); and
- the initial equity sale receipt and subsequent capitalised rent on the retained equity when the unit reverts to new build HomeBuy once the occupier has decided to purchase.

The initial net rent receivable is capitalised at an appropriate discount rate for an appropriate length of time to reflect the initial rental period. At the point the purchaser decides they want to purchase the unit, the unit is then valued using the same methodology as for new build HomeBuy, but deferred for the length of the initial rental period.

If the valuer assumes that staircasing will occur and that net receipts will be reinvested by a registered provider, this capital should be built into the cashflow and discounted back at an appropriate rate as set out in ‘RTA and Staircasing Receipts’ below.

Right to Acquire (RTA) and Staircasing Receipts

8.23 In England, the Housing Act 2004 (as amended) sets out provisions for qualifying tenants housed in properties that are eligible for RTA. The Homes and Communities Agency’s (HCA) Capital Funding Guide provides further detail on qualifying tenants and properties that are eligible.

8.24 In Wales these provisions also apply but (in 2010) the Welsh Assembly Government is considering suspension of the right to acquire in certain areas.

8.25 The HCA’s Capital Funding Guide sets out provisions for the majority of tenants housed in affordable housing delivered with a Social Housing Grant (SHG) to staircase out (i.e. acquire 100% of the property). The only exceptions are new build HomeBuy schemes for the elderly and rural restricted staircasing schemes.

8.26 The valuer will need to consider whether tenants will exercise their right to acquire or staircase up/out, and then make a judgment as to how a registered provider will treat these receipts.

8.27 The Capital Funding Guide provides guidance on the extent to which a registered provider is required to reinvest any receipts from RTA or staircasing, and what proportion it is able to use at its sole discretion.
8.28 A registered provider could use net RTA and staircasing receipts in one of the following ways:

- Make an assumption as to the level of net receipt on a scheme and input this into the cashflow in order to underpin an offer for the land.
- Make no assumption about this net receipt and just use it for other wider affordable housing business purposes as and when it accrues.

Consideration should also to be given to the possible extent of tenants exercising the Right to Acquire or staircasing up/out and their impact on the valuation.

**Outgoings**

8.29 Service charges can vary widely. The reasonable costs of management and maintenance and repairs are usually recoverable from the occupiers.

An allowance for bad debts is factored into appraisals of all Intermediate products with an element of rent that is payable (rent to HomeBuy, new build HomeBuy and Intermediate Rent). This is typically in the region of 5% of the rent receivable.

An assumed level of voids should also be built into the appraisal for Intermediate Rent and rent to HomeBuy accommodation to cover voids between tenancies. In the case of new affordable products such as rent to HomeBuy, there will be no existing evidence of typical void periods for the tenure, but assumptions can be made on the basis of typical void rates for comparable tenures (for example Intermediate Rent) in comparable areas.

**Other receipts**

8.30 Ground rents can be charged to occupiers of any affordable tenure or product but only on particular products (predominantly intermediate) are they recoverable from tenants. If the ground rent is not recoverable the registered provider will have to pay it themselves which will reduce the net rent and hence value. Where ground rents are payable by occupiers of new build HomeBuy, shared equity and discounted market sale units, they can be recouped by a registered provider from occupiers.

The value of any ground rent receivable is ascertained by capitalising the ground rent at an appropriate yield.

Other income such as receipts from occupiers from the sale of car parking spaces should also be included within the calculation of the GDV.

**9 External subsidies**

9.1 External subsidies may be available in the form of Social Housing Grant or by some other mechanism. Their availability and quantum is subject to change. When it is available SHG is a form of government subsidy allocated to registered providers to facilitate the provision of affordable housing.

9.2 In England any SHG allocated to a scheme can come from either:

- an allocation straight from the HCA’s National Affordable Housing Programme (NAHP), or other funding initiatives; or
- the Recycled Capital Grant Fund (RCGF).

9.3 In Wales the SHG system is directed by the Welsh Assembly Government and will differ from that in England.

9.4 RCGF comprises staircasing proceeds from New Build HomeBuy, land sales and property sales. These proceeds are then reinvested by the registered provider back into building affordable housing. When a registered provider applies for SHG on a site, any RCGF that they propose to use is treated by the HCA as ‘other public subsidy’ and is deducted from the total subsidy required to ensure the scheme is viable. The remaining shortfall in subsidy is filled by SHG.

9.5 There are a number of statutory and design criteria that affordable housing must satisfy in order for it to qualify for SHG. These design criteria are detailed in the HCA’s Design and Quality Standards (DQS) 2007, and are covered in paras 12.2 to 12.5 below.

9.6 In addition to the design criteria, the registered provider must demonstrate that the scheme is deliverable and the unit mix provided will go towards meeting local housing need and regional housing priorities. The registered provider must also ensure that the use of grant delivers value for money.

9.7 In some circumstances, SHG, and other subsidies, can be put into the cashflow as an additional revenue stream and can be envisaged as
9.8 The HCA has begun to explore equity funding in addition to capital funding. A consultation paper was issued in early 2010.

9.9 Viability appraisals are undertaken at a scheme level and the HCA have viability toolkits that assess the need for grant in delivering a target percentage of affordable housing. The results of these grants tend to be assessed by the HCA on a percentage of total scheme costs, or per person, or a per unit basis, or even all three for social rent and intermediate units. The per person allocation of SHG for social rent tends to be used in regions where central government is seeking to incentivise the provision of larger, family sized units for social rent through the allocation of SHG. Local authorities and practitioners also use proprietary and bespoke tools to appraise and negotiate the extent and nature of affordable housing in a s. 106 agreement.

9.10 Whilst not offering a subsidy the DCLG have issued a consultation document dated November 2009, relating to Rural Exception Sites as defined in PPS3: Housing. It seeks to establish ways of encouraging landowners to bring forward land for affordable housing by offering referral rights to nominated family members or employees to the tenancy of a percentage of the properties and/or the right to retain an interest in the land.

11 Internal subsidy

11.1 The primary function of a registered provider is to provide homes that are affordable for those in housing need. They are not for profit organisations and so will not, by and large, look to develop affordable housing at a surplus in the same way as a developer will build private housing.

11.2 Registered providers will develop certain tenures of affordable housing (for instance social rent) at a loss and may input cash from their own reserves in order to make an offer competitive. This is in keeping with their remit as not-for-profit housing providers. It is worth noting that any internal subsidy that a registered provider may provide on a site will be an opportunity cost to other aspects of their operation, such as maintenance or repairs.

11.3 In strong market conditions registered providers have looked to mitigate any deficit on social rent units through cross subsidising (offsetting a loss on one tenure by a surplus on another tenure) revenue from Intermediate tenure units.

11.4 The level of internal subsidy that a registered provider may put in to a scheme should be carefully considered when calculating the GDV. This is a difficult figure to measure and will vary between registered providers according to tenure priorities, market conditions and the specific opportunity. Registered providers will be more likely to provide internal subsidy for social rent as this tenure is considered less risky than Intermediate tenures. The actual figures assumed as internal subsidy should come from market evidence of subsidies provided by registered providers for specific tenure types in specific locations.

12 Establishing the development costs

12.1 Much of the Development Costs section of VIP 12 (para. 6.6) is applicable to this guidance note but further explanation is needed on the treatment of the following items when undertaking a valuation of land for affordable housing:
(a) Build costs
(b) On-costs/professional fees
(c) Finance
(d) Tax
(e) Cashflow of offer
(f) Developer’s profit

a) Build costs

12.2 Construction costs include the cost of building the residential units and any other associated site works or infrastructure costs. They include items such as materials and labour, as well as any remediation costs.

12.3 Affordable housing units have to comply with stringent standards if they want to secure SHG funding, although an increasing number of registered providers have adopted these as a minimum (regardless of the availability of SHG) and would expect all units to meet them.

12.4 In England these standards are specified by the HCA in their Design and Quality Standards (DQS), April 2007 (formerly known as Scheme Development Standards).

The DQS cover three broad areas:

- Internal environment – Assessed by Housing Quality Indicators (HQIs), (for example, unit size)
- Sustainability (for example, Code for Sustainable Homes)
- External environment (for example, Building for Life)

These standards are currently more rigorous (and therefore often more expensive) than the general Building Regulations with which private units have to comply. In determining relevant build costs, reference should be made to published indices such as BCIS and the surveyor’s past experience of working on comparable affordable schemes.

12.5 Any site specific factors such as the presence of contamination (and the associated cost of remediation or benefits of and remediation relief under s. 70 of the Finance Act 2001) and the location and design of the scheme (whether predominantly houses or flats, high rise or low rise) that may impact upon build costs should also be considered.

12.6 Affordable housing that is to be provided without SHG funding does not have to comply with the standards detailed above and therefore may be less expensive to construct. It is worth noting, however, that many registered providers require affordable housing to comply with DQS whether or not SHG funding will be sought.

12.7 In Wales the Welsh Assembly Government is seeking to achieve at least Code Level 3 on all new housing. The Welsh Housing Quality Standard has been developed to provide a common standard for the physical condition of all social housing in Wales. This is a minimum standard and will apply to all houses being transferred under stock transfer schemes. Design Quality Requirements are higher standards that RSLs must meet when delivering new units. As from 1 September 2009, all new housing of more than 5 units (as from 1 September 2010 all new housing) will need to achieve at least Code Level 3 of the Code for Sustainable Homes.

b) On-costs/Professional Fees

12.8 These are additional costs associated with the construction of affordable housing on a site. On-costs differ whether the appraisal is for a 100% affordable housing scheme or a s. 106 package of units.

12.9 The reason for the difference is that a number of costs (for example professional fees) will not be incurred by the registered provider if they are purchasing the units as part of a s. 106 obligation. In this scenario the registered provider is effectively purchasing a ‘turn-key’ deal of completed units from a developer with many of the costs being borne by the developer as part of the construction process.

c) Finance

12.10 Another important cost in producing a residual land value is the cost of finance. This is taken from market knowledge of the rates of borrowing that registered providers are contemporaneously securing in order to fund their developments. The majority of residual appraisals assume that a registered provider would borrow 100% of the money needed to fund the scheme.

12.11 In general, registered providers are able to secure more favourable rates of financing on their loans than private residential developers, as they are perceived by lenders to have government support and provide a predetermined exit route. Also attractive to a lender is a registered provider’s
ability to borrow against their large portfolios of existing stock that have relatively secure income streams from tenants who are often in receipt of government housing benefit.

d) Tax

12.12 Registered providers are generally treated differently from a private developer from the point of view of both tax relief and recoverability of VAT on fees.

12.13 Where a development is subject to a VAT election there are a number of options available to RSL to recover VAT. One such option is for the RSL to purchase the site only when construction has reached a point at which buildings, and not land, are being transferred. This is often referred to as a ‘golden brick’ payment. The particular circumstances will need to be established and reflected, as appropriate, in the valuation.

e) Receipts

12.14 When complying with a s. 106 package of affordable housing units registered providers may make payments up front and/or during construction. The impact of these on the funding required to finance the scheme and therefore the value of the land needs to be considered. The impact will vary between RSL and other providers.

f) Developer’s profit

12.15 On an appraisal of land for a 100% affordable housing scheme where a registered provider is acquiring the land directly, it should be assumed that as the registered provider is acting as the developer it will not seek to make a profit. Therefore no allowance should be made for developer’s profit.

12.16 A registered provider may build in a surplus for one tenure type on a scheme, but this will generally be to offset a loss on another tenure being provided at the scheme, and should not be treated as a profit.

12.17 For an appraisal of a s. 106 package of affordable housing units a level of profit should be assumed to reflect the risk to a developer of the sale to a registered provider of the s. 106 affordable housing units.

13 Non-HCA compliant affordable housing

13.1 PPS3 allows for affordable housing needs to be met by organisations who fall outside the remit of the HCA’s regulatory framework.

13.2 Detailed previously is the HCA compliant method of delivering affordable housing. In England, in order to access SHG from the HCA, affordable units must comply with the regulations and restrictions discussed. In Wales SHG is only available to RSLs.

13.3 However, there are some house builders involved in the delivery of affordable housing that do not utilise SHG. A number of these companies offer variations on intermediate tenure products but, because they do not need to access SHG, there is more flexibility in how value can be generated.

13.4 Whilst similar products to intermediate rent and new build HomeBuy are offered they are not subject to the same restrictions. For instance, in the case of new build HomeBuy, companies may offer smaller initial equity shares than 25% or may charge a higher rent on the retained equity than the limits imposed by the HCA.

13.5 In the case of a discounted market sale, the GDV is driven by the initial equity sale, in much the same way as the sale of a private unit on the open market.

13.6 Whilst a number of companies offer these products, they are dependent upon local authorities approving their use and they are subject to planning restrictions if these products are intended by developers to comprise all or part of the s. 106 affordable housing obligation.

14 Establishing the land value

14.1 Where a comparative approach is followed the land value is determined at an early stage. However, the valuer may wish to check the result against a simplified residual valuation, or consider if any of the factors explicit within a residual valuation (such as specific planning or site characteristics), have been appropriately reflected in any adjustments that have been made to the comparables.
14.2 Where a residual approach has been followed the valuer draws together the various elements and, having established the completed value, by deduction of the various costs, determines the maximum price that the RSL can pay for the land. It is a matter of judgment as to whether or not this figure represents the Market Value of the land.

14.3 Care should be taken over how any subsidies are treated in establishing the residual value. In certain cases it may be appropriate for a level of subsidy to be incorporated within a valuation if, for example, their presence is either included as an assumption or special assumption, or, in the case of a calculation of worth, they are specific to a particular registered provider. In general, it will not be appropriate to assume that subsidies will be available to, or supported by, a registered provider and so they should not be included within the valuation.

14.4 If the valuation is of a s. 106 package of affordable housing units, then the overall residual value of the units should be calculated in line with the methodology detailed in this guidance note. This residual value should then be incorporated into the overall scheme appraisal and treated as the GDV (or revenue) that a private developer could expect to receive from a registered provider for the affordable element of a scheme.

15 Reporting the valuation

15.1 The precise format of the report depends upon the instructions given and its purpose but regard must be had to the requirements of PS 6.1(a) to (s) and in particular:

- the basis of value must be clearly stated (PS 6.1(f));
- all the assumptions, including any special assumptions, made must be stated (PS 6.1(k)). The effect of any assumptions that have a material effect on the valuation need to be commented upon; and
- the statement requiring comment on the valuation approach is particularly important in the valuation of these assets (see PS 6.1(q)).

15.2 It may be appropriate to present an appraisal based on provable values alongside a sensitivity analysis to show the effect on the land value of differing assumptions as to factors such as future estimated values, availability of SHG and different levels of a registered provider’s internal subsidy. The aim is to assist the client in assessing the land value by reference to different potential scenarios of shifts in both market practice (amount of subsidy) and policy changes (availability or otherwise of SHG). In these instances and in common with all other valuation exercises valuers need to be transparent about their approach and, particularly when reporting for loan security purposes, these elements of the reported value are to be identified separately.

15.3 Should the land have a negative value, even if it is not to be developed, the negative value must be reported in accordance with PS 6.8.

15.4 If an alternative use can be made of the land that produces a higher value that should be reported together with any relevant assumptions made in arriving at that conclusion.

15.5 Where the purpose of the valuation is not one where a single figure valuation is required it is acceptable to agree with the client that a range of values be reported, particularly where the report includes a sensitivity analysis, with an explanation of the reasons for the range adopted.
Appendix A: Glossary of terms

**Code for Sustainable Homes (CSH)**
A system of scoring and benchmarking affordable housing developments in terms of their environmental impact. The scoring is currently graded by levels (from 1–6). In order to qualify for grant funding new affordable homes must meet level 3 as a minimum. Registered providers are incentivised to achieve higher CSH ratings through the potential for securing additional SHG. This system is not used in Wales.

**Discounted Market Sale**
An intermediate tenure product that sees the registered provider or developer offer the unit for sale to prospective purchasers (who meet specific affordability criteria) at a specified discount to the market value of the unit. This is typically around 80% of market value, with the purchaser buying the whole 80%. In order to ensure that these units are maintained as affordable into perpetuity, when the purchaser sells the unit on, it must be at 80% (or whatever the original percentage purchased was) of the current market value.

The provision of discounted market sale is driven by local policy, where a local authority may accept the provision of this product as part of the affordable housing obligation. Often covenants will be built into discounted market sale leases to ensure that if the property is re-sold in the future the discount to market value is maintained into perpetuity.

**Homes and Communities Agency (HCA)**
The HCA was formed in December 2008 as a result of the merger of English Partnerships and the Housing Corporation. Its remit is limited to England. The HCA is responsible for delivering the majority of England’s affordable homes through providing funding (SHG) for registered providers to develop new homes. All new affordable homes funded by SHG must meet minimum quality and design standards, including sustainability levels and minimum room sizes in excess of those required in the private sector.

The HCA is also responsible for overseeing improvements to existing affordable homes.

**Housing for Rent**
Housing for rent covers those affordable housing types that are purely for rent and do not have a sale element to them. This includes social rented tenure and the intermediate rent and rent to HomeBuy types that are intermediate tenure.

**Housing for Sale**
Housing for sale covers those affordable housing types where occupiers have the opportunity to purchase a stake in their home. The types of housing that fall under this category are intermediate tenure and include new build HomeBuy, right to acquire, shared equity.

**Housing Quality Indicators (H奎)**
A measurement and assessment tool designed to allow housing schemes to be evaluated on the basis of quality rather than simply cost. It is used by the HCA and considers 10 key features (divided into individual indicators) of a housing project broken down into three main categories, covering location, design and external environment. Minimum threshold scores apply to qualify for SHG.

**Intermediate Housing**
Housing that is at prices and rents that are above those of social rent, but below market price or rents, and that meet local affordability criteria that will enable people unable to access market housing to afford them. The affordability criteria are set by local authorities and are typically related to the amount that a person can afford, as a percentage of their gross income to spend on housing costs.

Intermediate tenure can include a number of products that have an element of equity sale, or are purely for rent.

**Intermediate Rent**
An intermediate tenure product where an occupier pays a rent to the registered provider (who retains full ownership of the unit) that is above that of social rent and is more closely related to the market rental value of the unit. How much a tenant should pay is related to specific affordability criteria within a local authority (i.e. the maximum incomes prospective tenants should have in order to qualify)
but the HCA designate that the maximum a tenant can pay is 80% of market rent.

**New build HomeBuy**

Formerly known as shared ownership, this is an intermediate tenure product whereby an occupier purchases an initial percentage (or tranche – usually a minimum of 25%) of equity in their home and pays an annual rent as a percentage of the retained equity to the registered provider.

Occupiers will have future opportunities to purchase additional tranches (known as ‘staircasing’) from the registered provider. The occupier will often have the opportunity to staircase up to 100% ownership, but some new build HomeBuy occupiers are capped at a maximum of up to 80% ownership by restrictions in s. 106 agreements (especially in rural locations).

**Registered Providers**

Those organisations which can be either profit making or non-profit making and satisfy the criteria detailed in Chapter 3 of the Housing and Regeneration Bill 2008.

In the main, registered providers are not for profit organisations but can include private developers who have satisfied the criteria of the Homes and Communities Agency and are eligible to bid for and receive HCA grant funding.

**Rent to HomeBuy**

An intermediate tenure product where new build homes are rented on an Intermediate Rent basis for up to a maximum of five years, after which the occupier has the opportunity to purchase the home through the new build HomeBuy scheme.

There are a number of different incentives being offered by registered providers to encourage the occupier to purchase at the end of the rental period. These are:

- a percentage of the rent that the occupier has paid is returned to them to help use as a deposit;
- the registered provider matches the savings that an occupier has accumulated over the rental period in order to use as a deposit; and
- the registered provider gives the occupier a lump sum (according to length of occupation) to help with a deposit.

**Right to Acquire (RTA)**

Right to Acquire offers qualifying tenants of qualifying properties the opportunity to purchase their home at a discount. The discount is a fixed sum of money that varies geographically.

The legislation on Right to Acquire is contained in the *Housing Act* 2004 (as amended).

**Shared Equity**

Similar in principle to new build HomeBuy, an intermediate tenure product whereby an occupier purchases an initial percentage (or tranche) of equity in their home. Shared equity differs from new build HomeBuy in that the occupier does not pay rent on the equity they do not own.

**Social Housing Grant (England)**

The funding provided by the HCA to Registered Providers to support the delivery of affordable housing. SHG is allocated to specific developments and is paid under s. 18 of the *Housing Act* 1996. Traditionally, SHG has been paid as capital or ‘gap’ funding, but the HCA is in the process of changing its investment model and to looking to provide grants in the form of equity investment.

**Social Housing Grant (Wales)**

A grant given to Registered Social Landlords by the Welsh Assembly Government. The grants aim to provide new affordable housing for rent or low cost home ownership.

**Social Rent**

This is rented housing that is owned and managed by local authorities and registered providers. The rents are regulated by the HCA in order to keep them affordable to residents within a local authority and differ according to the unit size, market value of the unit and relative county earnings. The rents are subject to a rent cap, set by the HCA, that can track RPI movement + 1% per annum.

**Staircasing**

Staircasing is the process of purchasing additional shares of a new build HomeBuy property.

Depending on the terms of the shared ownership lease, there may be restrictions on the timing and amount of staircasing, but in general it is possible to buy 10% minimum tranches until the purchaser has reached full ownership.
The cost of staircasing is determined by a valuation of the property at the time the purchase takes place. In order to calculate this in the discounted cashflow the projected market value of the completed unit at the time of staircasing should be discounted back to the present day in order to form part of the overall GDV.

Once the buyer has purchased 100% of the property, they own it outright (typically on a long lease in the case of flats and freehold for a house), and are no longer liable to pay rent to the registered provider.
Valuation of land for affordable housing
1st edition, guidance note

The provision of affordable housing has been high on all political agendas for many years but there has been limited guidance to valuers on the methodology behind the valuation of land for that purpose.

This guidance note aims to assist the valuer in the approach to the valuation of land for affordable housing by focussing on the affordable housing element of a scheme.

Although the methodology behind the valuation of land for affordable housing has much in common with a conventional valuation of development land, it can be very complex as it relates to specialised markets. These valuations therefore require a high level of expertise.

The main topics covered are:
- What is affordable housing?
- Establishing the facts and development potential
- Methods of valuation
- The approach to a residual valuation
- The impact of subsidies
- Reporting the valuation.

This guidance has been prepared with regard to valuation practice in England and Wales.