10 May 2024

Padraig Scollard
Keylan

Sent via email: padraig@keylan.com.au

Dear Padraig

Re: 159-167 Darley Street West, Mona Vale - Affordable Housing Viability Assessment Peer Review

Atlas Economics (**Atlas**) is engaged by Keylan on behalf of Department of Planning, Housing and Infrastructure (**DPHI**) to undertake a peer review of Affordable Housing Viability Assessments prepared for a planning proposal at 159-167 Darley Street West, Mona Vale (**the Site**). This is to assist with the setting of an appropriate Affordable Housing contribution rate.

BACKGROUND

Intrec Management (**the Proponent**) lodged a planning proposal (**the Proposal**) with Northern Beaches Council (**Council**) in July 2021. The Proposal sought to enable development of residential flat buildings and townhouses (3,683sqm GFA).

Table 1 outlines the planning controls under the Pittwater Local Environmental Plan (**LEP**) 2014 that currently apply to the Site and the amendments sought by the Proposal.

Table 1: Current and Proposed Controls

Control	Current	Proposed
Zone	R2 Low Density Residential	R3 Medium Density Residential
Maximum height of building	8.5 metres	No change
Floor space ratio	Not applicable	No change
Number of dwellings	5 (existing single dwellings), 10 (potential dual occupancy)	41 dwellings comprised of: • 38 apartments - 1b (12), 2b (20), 3b (6) • 3 townhouses

Source: Planning Proposal

In March 2023 the Proposal made a voluntary planning agreement (**VPA**) offer to contribute to Affordable Housing at a rate of 2.085% (equivalent to $1,122,627). The offer was supported by a feasibility analysis by Macroplan (**the Macroplan Study**).

Separately, Council engaged Hill PDA to undertake a review of the Macroplan study and provide advice on an appropriate Affordable Housing contribution assuming the proposed planning control amendments were made (**the Hill PDA Study**).

In September 2023 a Gateway Determination was issued for the Proposal. At the pre-Gateway briefing, the Sydney North Planning Panel (**the Panel**) determined that the contribution be increased to 5% and required through a new Affordable Housing clause in the LEP and associated Affordable Housing Contributions map.

Atlas Economics (**Atlas**) is engaged to carry out a peer review of the Macroplan Study and the Hill PDA Study and provide advice on an appropriate Affordable Housing contribution rate. This Peer Review reviews both studies and undertakes its own feasibility testing in arriving at a recommended Affordable Housing contribution rate.

AFFORDABLE HOUSING POLICY

Greater Sydney Region Plan and District Plans (2018)

The Greater Sydney Region Plan and North District Plan identify affordable housing targets of 5%-10% of *new* residential floorspace (that is, floorspace resulting from a rezoning), subject to viability. The Greater Cities Commission (**GCC**) issued Information Note 4 (GSC, 2017) to clarify application of the Affordable Rental Housing Targets.

The GCC proposed Affordable Rental Housing Targets to apply as follows:

- apply to land that is the subject of upzoning - a change of land use to residential or an increase in permissible residential development density.
- vary by precinct according to the local development viability.
- apply only to new areas nominated by the relevant planning authority; not apply retrospectively to rezoned land.
- be announced prior to rezoning to give the market certainty about the amount of affordable housing to be provided, and so that it can be factored into underlying land prices.
- apply to land within new urban renewal or land release areas (govt and private) identified via a local or district housing strategy, or another form of appropriate research that illustrates a current or future need for affordable rental housing.
- be calculated as a proportion of all residential floor space above the base floor space ratio - that is, the residential floor space ratio that was permissible before the upzoning within the nominated area.

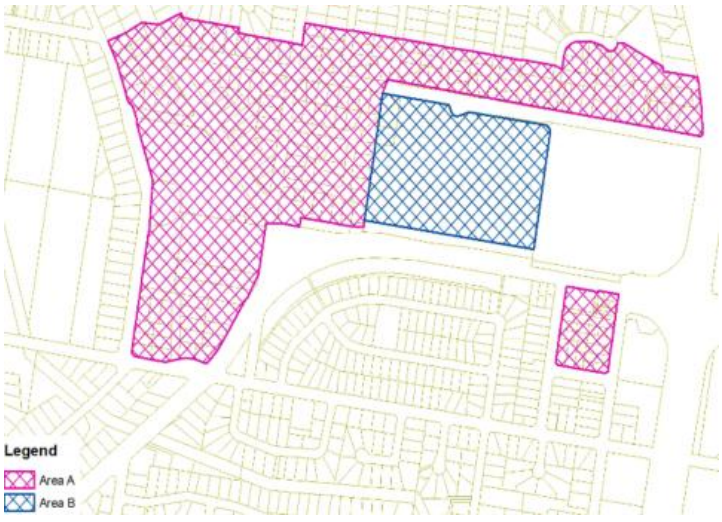
Information Note 4 provides some parameters for an approach to development feasibility testing, including that the testing should consider "*the feasibility of residential development, with a normal risk/ return margin, including the cumulative costs of local, and where appropriate State contributions*".

Atlas notes that both studies (Macroplan and Hill PDA) identify that Affordable Housing contributions should be on 'new' floorspace. However, they deduct 'existing/ built' floorspace, rather than permissible floorspace under the current controls.

Northern Beaches Affordable Housing Contributions Scheme (2019)

The Northern Beaches Council (**Council**) Affordable Housing Contributions Scheme (**the AHCS**) applies in the Frenchs Forest Planned Precinct (**Figure 1**) and specified sites in Narrabeen.

Figure 1: Frenchs Forest Planned Precinct - Affordable Housing Contribution Rate Areas



Source: Northern Beaches Council (2019)

Affordable Housing contributions are required depending on the area of a development (shown in **Figure 1**):

- In Area A (private land) - dedication free of cost to the consent authority - 10% of gross floor area (GFA) is required.
- In Area B (the Forest High School) - dedication free of cost to the consent authority - 15% of GFA is required.

The application of the 10% rate in Area A does not acknowledge the residential floor space ratio that was permissible before the rezoning. Rather, contributions are required on total floorspace, not just on the floorspace enabled by the rezoning.

PEER REVIEW OBSERVATIONS

Atlas generally agrees with the assumptions taken by both studies. Since their preparation, new fees and charges have come into effect and should accordingly be included in the feasibility testing.

Table 2 selects key feasibility assumptions for comparison and comment.

Table 2: Feasibility Assumptions - Comparison and Comment

Assumption	Macroplan	Hill PDA	Atlas comment
Cost of Land	$16,524,000	$16,535,000	Agrees with and adopts Macroplan assumption
Sales Revenue	$65.82m (excl. GST)	$70.34m (incl. GST)	It is market practice for residential revenues to be quoted inclusive of GST. Sales commissions and GST are thereafter deducted from these revenues. Atlas considers the revenue rates generally appropriate and adopts: • 1 bedroom unit - $1,028,500 • 2 bedroom unit - $1,815,000 • 3 bedroom unit - $2,530,000 • Townhouse - $2,860,000 After multiplying with the proposed residential yield (per the Planning Proposal), a gross sales revenue (incl. GST) of $72.4m results. This is equivalent to $65.82m (excl. GST) the same as Macroplan's assumptions.
Build Cost and Contingency	$25,581,327 ($6,946/sqm GFA)	$22,762,320 ($6,180/sqm GFA)	Atlas concurs with Hill PDA's comment that the build rate of $4,800/sqm is well above Rawlinsons and RLB generic rates. Notwithstanding, in the current inflationary cost environment, this rate is adopted. The basement construction rate of $50,000 per space would appear low. Atlas adopts a rate of $60,000 per space. The above rates result in a build cost of $23,182,320 (including 5% contingency), which is equivalent to $6,294/sqm GFA. While Atlas are not quantity surveyors, from past industry experience, this build cost rate (before professional fees and statutory fees) is considered appropriate, if not conservative, for a development of 8.5m (<3 storeys). Additional allowances for site works are not separately made. This could be required if there are extraordinary site conditions (e.g. geotechnical or contamination constraints).

Statutory Fees and Charges	$255,813	$303,498	The studies appear to only allow for s7.12. Atlas additionally allows for:
			• Housing and Productivity contributions (at 75% from 1 July 2024)
			  ◦ $12,000 per house
			  ◦ $10,000 per apartment
			• Sydney Water DSP charges (at 25% from 1 July 2024)
			  ◦ $5,663.60 per ET (drinking water and wastewater)
			  ◦ 1 ET per house, 0.8 per ET per apartment

Construction Period	24 months	16 months	Atlas considers 16 months to be possibly too tight, adopting an 18-month construction period. A lead-in period of 18 months is assumed prior (to allow for DA approval, documentation and pre-sales).
Interest Rate	10% pa	7.5% pa	The latest RBA data would suggest inflation has peaked. While rate cuts are not imminent, there is generally a market consensus that rates have peaked and they could start to fall in 2025/ 2026. Atlas adopts an interest rate of 8% pa, which is considered to be conservative for when the project is expected to commence and require project finance (2025).
Holding Costs	$330,000	$600,000	Holding costs are estimated at $475,000 through searches of land tax, Council rates and fixed water rates.
Affordable Housing Contributions	$1,122,627	$3,374,872	Both studies iteratively test different % contribution rates on the proposed GFA less 'existing/ built' GFA. This is contrary to the GCC's guidance on how Affordable Housing contributions are to be calculated.

Source: Atlas

As an overall observation, assumptions in the two studies are mostly aligned except on build cost and contingency where there is an almost $3 million difference. Atlas considers the Macroplan assumptions to be conservative; we adopt the build cost (and increase the basement parking cost) but do not make separate allowances for site works. There may however be extraordinary site conditions unknown to Atlas, which could require revisiting of the construction cost assumptions.

ATLAS' FEASIBILITY TESTING

The objective is to test that if after making Affordable Housing contributions, development still achieves commercial returns.

The feasibility testing uses the Residual Land Value (RLV) method, similar to the approach both studies have taken. This method assesses the potential revenue on completion of the development, deducts development costs and makes a further deduction for profit and risk that a developer and financier would require to take on the project. If the project return and development margin are above minimum hurdles, the development is considered feasible.

The RLV can be defined as the maximum price a developer would be prepared to pay for a site in exchange for the opportunity to develop a particular development scheme whilst achieving target hurdle rates for profit and project return. For a development to be considered feasible, the RLV must exceed the Site's 'base land value' or opportunity cost of land.

Assumptions and Limitations

Atlas acknowledges the assumptions and limitations associated with the feasibility testing.

- Market research is carried out on a 'desktop' basis without the benefit of site surveys and internal inspections.
- Construction prices have increased significantly (circa 20%-30%) over the past 24 months across the country.
- Atlas expects project delivery to occur over 2-4 years (from DA lodgement to completion). Market commentators expect construction cost escalations to begin stabilising in 2025. This does not mean costs will reduce, merely that annual increases return to trend (~3%). In the circumstances, the cost assumptions are considered appropriate.

Lenders require mortgage valuations to assume certain hurdle rates; while market appetite may vary with development/ market cycles, capital finance requirements do influence the parameters within which a development project is 'bankable'.

Table 3 outlines the target hurdle rates adopted for the feasibility testing.

Table 3: Benchmark Hurdle Rates

Hurdles	Feasible	Marginal	Not Feasible
Development Margin	>20%	18%-20%	<18%
Project Return (IRR)	>18%	17%-18%	<17%

Source: Atlas

Affordable Housing Contributions

Any assessment of Affordable Housing contributions is underpinned by the considerations of Information Note 4, that is, the Affordable Housing Targets are calculated as a proportion of residential floor space ***above*** the base floor space ratio.

The Site measures 6,120sqm and is subject to an 8.5m height limit. There is no floor space ratio. While current improved with five single dwellings, dual occupancy is permitted in the zone and thereby the Site has a dwelling potential of 10.

The Planning Proposal seeks to amend the LEP to permit 41 dwellings, thereby resulting in 31 dwellings enabled by the rezoning. **Table 4** shows the quantum of Affordable Housing that could result from 5% and 10% of the 31 'new' dwellings.

Table 4: New Residential Floorspace from Rezoning

	Before Rezoning	Planning Proposal
Dwellings potential	10 (dual occupancy)	41
New dwellings (enabled by Planning Proposal)		**31**
5% x 31 new dwellings (% of 41 dwellings)	n/a	1.55 dwellings (3.8%)
10% x 31 new dwellings (% of 41 dwellings)	n/a	3.1 dwellings (7.6%)

Source: Atlas

Depending on the percentage contribution, the quantum of Affordable Housing is equivalent to:

- 5% of 31 dwellings - 1.55 dwellings, which is approximately 3.8% of the 41 proposed dwellings.
- 10% of 31 dwellings - 3.1 dwellings, which is approximately 7.6% of the 41 proposed dwellings.

The feasibility modelling tests the impact of the above contributions on the feasibility of development.

Solving for Viable % Affordable Housing Contributions

This section tested Affordable Housing contributions - at 5% and 10% of 'new' dwellings (1.55 and 3.1 dwellings respectively) and found that it was viable to contribute 1.55 dwellings but not 3.1 dwellings. The testing found that development had the capacity to contribute more than 1.55 dwellings.

Testing was then iteratively carried out to solve for the number of dwellings (more than 1.55 dwellings, but fewer than 3.1 dwellings) that would be viable. The testing found that 2 dwellings was a viable contribution (which was equivalent to 5% of the 41 dwellings proposed).

Table 5 shows the % scenarios that were tested.

Table 5: Viability of Varying Levels of Affordable Housing Contributions

Dwellings	% Affordable Housing		Feasible?
(a)	(b) = (a ÷ 31 dw)	(c) = (a ÷ 41 dw)	(d)
1.6 dw	5% (x new floorspace)	3.8% (x total floorspace)	Yes
3.1 dw	10% (x new floorspace)	7.6% (x total floorspace)	No
2.0 dw	6.5% (x new floorspace)	5.0% (x total floorspace)	Yes

Table 6 shows the feasbility of development ***after*** Affordable Housing contribution of 2 dwellings is made. The target hurdle rates are achieved and the residual land value is greater than the Opportunity Cost of Land.

Table 6: Modelling Results

		5% total floorspace (6.5% new floorspace)	
Total Dwellings ('New' Dwellings)		41 dwellings (31)	
Affordable Housing Dwellings		2 dwellings	184sqm GFA (3,683sqm x 5%)
Gross Revenue (41 dwellings) ($/sqm GFA)		$72,402,000	$1,765,902/dw $19,658/sqm GFA
Revenue			**$/dw**
Gross Sales Revenue (revenue from 2 dwellings foregone)		$68,781,900	
Less: Selling Costs		($2,124,957)	
Total Revenue (before GST paid)		$66,656,943	
Less GST paid on revenue		($6,252,900)	
Total Revenue (after GST paid)		$60,404,403	
Costs			**$/dw**
Land Purchase Cost (Opportunity Cost of Land)		$16,524,000	$403,024
Transaction Costs		$974,495	
Construction Costs (incl. Contingency)		$23,182,320	$565,422
Professional Fees		$2,525,269	
Statutory Fees		$642,932	
Land Holding Costs		$475,875	
Finance Charges		$175,000	
Interest Expense		$5,458,567	
Total Costs (net GST)		$49,958,458	$1,218,499
Performance Indicators			**$/dw**
Development Margin	(a)	20.1%	
Project Return	(b)	18.1%	
Residual Land Value (excl. GST)	(c)	$16,566,128	$404,052
Analysis of Residual Land Value (RLV)			
Comparison to Opportunity Cost of Land	(d)	$16,524,000	
Feasible?	yes if (c) > (d)	Yes	

The modelling shows that a 5% Affordable Housing contribution (of the overall 41 dwellings) is viable. This is equivalent to:

- 2 average dwellings in aggregate terms (41 dwellings x 5%).
- 184sqm GFA in aggregate terms (3,683sqm GFA x 5%).
- 6.5% of the 31 'new' dwellings enabled by the rezoning.

Performance indicators achieve the target hurdle rates and the development is considered to be feasible. Atlas highlights that the feasibility testing is undertaken in a zero-escalation model and represents a conservative scenario. Should achievable revenues strengthen relative to construction cost, the feasibility outcomes would be more favourable than shown here.

For a full list of feasibility testing assumptions refer to SCHEDULE 1.

SUMMARY OF FINDINGS

The Study finds that there is an opportunity for the Proposal to contribute to 6.5% Affordable Housing (calculated on 'new' dwellings, i.e. the dwellings enabled by the rezoning) ***and*** remain viable. In overall dwelling terms, this is equivalent to 5% of total dwellings. This would be in line with the Panel's determination that a 5% Affordable Housing contribution should be made.

The Macroplan study raises concerns about the inclusion of an LEP clause to require Affordable Housing and the consequent inability of a development to respond to changes in project viability over time. Whilst this may be true, the same could be said of the proposed planning amendments (to be made in the LEP). For example, if material and labour shortages were to persist or if economic conditions become more unfavourable, the deterioration of project viability could require additional dwellings to the 41 dwellings sought.

Contribution Rates and Dwellings

Should Council seek dedication of dwellings, dedication of an average of two dwellings (or 184sqm GFA) that are valued at approx. $3,531,805 (in $2024 dollars) could be acceptable.

Compared to the contribution of dwellings in-kind, a monetary contribution would have a larger cashflow implication given its requirement earlier in the development, i.e. when s7.12 levies are payable. Notwithstanding, given the relative small scale of the development, the proponent could elect to make a cash contribution, rather than dedicate completed dwellings. The feasibility testing has assumed an aggregate 'average dwelling' which is a blend of 38 apartments and 3 townhouses. The equivalent monetary contribution would be the market value of 184sqm residential GFA.

Table 7 indicates the contribution in equivalent amounts in dollar terms and in completed/ built dwelling terms and when they would be contributed.

Table 7: Affordable Housing Contribution

	Completed Dwellings	Equivalent Monetary Payment
Affordable Housing Contribution	2 average dwellings (184sqm GFA)	$19,658/sqm GFA ($23,127/sqm NSA)
Timing of Contribution	End of development	Together with s7.12 Levy

Source: Atlas

We trust this assists DPHI with the setting of an Affordable Housing contribution rate. Please contact the undersigned with queries.

Yours sincerely

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Reference List

Greater Sydney Commission (2017). *Affordable Rental Housing Targets Information Note 4. Revised October 2017*. Accessible here: https://greatercities.au/sites/default/files/2023-07/information_note_4_affordable_rental_housing_targets_updated_october2017.pdf

Hill PDA (2023). *Affordable Housing Feasibility Analysis*. March 2023. Accessible from: https://www.planningportal.nsw.gov.au/ppr/post-exhibition/159-167-darley-street-west-mona-vale

Macroplan (2023). *Feasibility Analysis of Affordable Housing Contribution*. March 2023. Accessible from: https://www.planningportal.nsw.gov.au/ppr/post-exhibition/159-167-darley-street-west-mona-vale

Northern Beaches Council (2021). Affordable Housing Contributions Scheme. Accessible from: https://eservices.northernbeaches.nsw.gov.au/ePlanning/live/Common/Output/LoadGenWebDoc.ashx?id=HBWUDC3VbgIV0A60ki4OEg%3d%3d

SCHEDULE 1

Feasibility Testing Assumptions

Project Timing

The Site is assumed to be rezoned, with the cost of the rezoning assumed to be 'sunk' in Month 0 on purchase of the Site.

Pre-sales marketing commences in Month 9. Site preparation commences in Month 15 and construction is 18 months. Sales are completed by Month 36.

Indicative Residential Yield

Development yields are indicative and extracted from the Planning Proposal in **Table S1-1**.

Table S1-1: Indicative Residential Yield

Dwelling Type	Dwellings	GFA (sqm)
1 bedroom unit	12	3,266sqm
2 bedroom unit	20	
3 bedroom unit	6	
Townhouse	3	417sqm

Source: Macroplan

Revenue

Average end sale values are adopted from a review of the Macroplan and Hill PDA studies.

Table S1-2: End Sale Values ($2024)

Dwelling Type	Dwellings	End Sale Value
1 bedroom unit	12	$1,028,500
2 bedroom unit	20	$1,815,000
3 bedroom unit	6	$2,530,000
Townhouse	3	$2,860,000
	41	**Avg. $1,765,902**

Source: Atlas

Other revenue assumptions:

- GST is included on the residential sales.
- Sales commission at 2% (residential) gross sales.
- Marketing costs of 1% on gross sales and legal cost on sales included at $1,500 per dwelling.

Costs

- Land purchase cost imputed by the Opportunity Cost of Land ($16,524,000).
- Legal costs, valuation and due diligence was assumed at 0.5% of land price and stamp duty at NSW statutory rates.
- Construction costs are assumed based on review of Macroplan and Hill PDA studies:
    - Demolition - $200,000
    - Residential building - $4,800/sqm GFA
    - Basement parking - $60,000 per space
- Construction contingency of 5%.

Other cost assumptions include:

- Professional fees at 9% of construction cost.
- Development management at 1% of construction cost.
- Statutory fees:
    - DA and CC fees at Council's fees and charges.
    - s7.12 contributions at 1% of cost of development.
    - Housing and Productivity contributions at $12,000 per house and $10,000 per apartment (assumed at 75% from 1 July 2024).
    - Sydney Water DSP charges at $5,663 per equivalent tenement (assumed at 25% from 1 July 2024).
    - Long service levy at 0.25% of construction cost.
- Land holding costs applied at statutory rates (land tax, Council rates, water rates).
- Finance costs:
    - 100% debt funding at interest capitalised monthly at 8% per annum.
    - Establishment fee at 0.35% of peak debt.

Hurdle Rates

Key performance indicators relied upon are hurdle rates (development margin[1] and project IRR[2]). Benchmark hurdle rates and their 'feasible' ranges are indicated in **Table S1-3**.

Table S1-3: Benchmark Hurdle Rates

Performance Indicator	Feasible	Marginal to Feasible	Not Feasible
Development Margin	>20%	18%-20%	<18%
Project Return (IRR)	>18%	17%-18%	<17%

Source: Atlas

[1] Development Margin is profit divided by total costs (including selling costs)
[2] Project IRR is the project return on investment, the discount rate where the cash inflows and cash outflows are equal