TOPICAL ISSUES PAPER

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CITY OF LONDON

Prepared for the City of London Corporation
by Quod Research
Published November 2011

Relaxation of Planning Rules for Change of Use from Business to Residential:

Implications for the City of London

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CONTENTS

EXECUTIVE SUMMARY

1. The continued success of the City of London as the world's leading financial centre could be threatened by proposed changes to the Town and Country Planning (General Permitted Development) Order, which would allow uncontrolled change of use from business use to residential use. That change has the potential to undo the achievements of more than 30 years of town planning strategies which have been successively endorsed by Planning Inspectors and the GLA.

2. The City is unique in hosting a planned concentration of business and supporting uses. Whilst residential use is an important element of the City, it is deliberately planned for on the City fringes. The density and intensity of business use is essential for the 24/7 operation of the City and for its ability to renew itself through large scale redevelopment, which allows the City to continually adapt to suit the changing needs of business. The existence of residential uses removes this essential flexibility.

3. Evidence shows how sporadic residential uses can remove the ability of the City to adapt through preventing development due to their longer lease structures and inhibiting its scale through their entitlement to rights of light and privacy. Residential rights also impose costly controls on the early and late servicing and operational activity which is essential for maintaining a competitive business environment.

4. An analysis by agents Jones Lang LaSalle has advised that residential values often exceed office values at different times in the economic cycle (including the current time), with the consequence that as much as 13m sq ft of office floorspace could be at risk from the proposed relaxation in the short term.

5. The proposed changes, therefore, have the clear potential to undermine the City of London's unique and essential contribution to the UK economy.

6. No other part of the country has the characteristics of the City – the City could and should be excluded from the proposed changes.

INTRODUCTION

1. The Government has consulted on proposals to change the Town and Country Planning (General Permitted Development) Order, so as to grant a general permission for Business premises in Use Classes B1, B2 and B8 to be used for residential purposes, without the need for planning permission. The Government is now considering the outcome of consultation. This Paper makes the case for excluding the City of London from that general permission.

2. The City of London has unique characteristics which make it distinct from any other part of the country and which allow it to perform the vital role of hosting and driving the country's growth as the world's leading financial centre. The ability to focus core areas of the City on this unique role is essential and a general grant of planning permission, which allowed uncontrolled change of use of business premises to residential use in the heart of the City, would severely inhibit the ability to meet the 24/7 operating requirements of existing tenants or the growth requirements of those new businesses which the City must be able to serve. Given the strength of international competition it would be directly contrary to the national interest if the City of London was unwittingly handicapped in this way.

3. The proposed amendments to the Town and Country Planning (General Permitted Development) Order can achieve their purpose nationally without applying them to the City of London. This is a geographically small area, where the benefits of relaxation are likely to be relatively small in terms of residential uses generated, but would have seriously adverse consequences in terms of the harm that would be done to the integrity and future of the City.

4. These propositions are explained in this Paper under a series of headings, as follows:

   - The unique character and contribution of the City of London;
   - The value of the City of London as the world's premier business cluster;
   - The agreed need to control residential use in the City;
   - The risks of relaxation;
   - Suggested amendments to the reforms.

THE UNIQUE CHARACTER AND CONTRIBUTION OF THE CITY OF LONDON

5. The City of London Core Strategy was formally adopted in September 2011. It describes the City as follows:

   "2.1 *The City of London is unique. Although little more than one square mile in size, it is densely developed and is the world's leading international financial, business and maritime centre. It is a leading driver of the London and national economies. It provides employment for over 370,000 people who mostly use public transport to commute to work from across London and the surrounding regions. Offices* *make up over 70% of all buildings and many of them are occupied by financial and business services."*

6. London is a leading world financial centre and in September 2011 was rated 1st ahead of New York, Hong Kong, Singapore and Shanghai (Source Z/Yen Global Financial Centres Index September 2011). London has topped this ranking since the first GFCI publication in 2007.

7. The City of London is at the heart of London's financial and business services activity and is home to many of the world's leading markets, e.g. London Stock Exchange, London International Financial Futures and Options Exchange (LIFFE), Lloyds of London Insurance Market, London Metal Exchange, ICE Futures Europe. The City of London's financial and professional services are estimated to have contributed £32bn to national output in 2010.

8. Other areas of London and the UK, of course, also make significant contributions but none operate at the scale or density of the City. The City's employment in financial, insurance and professional services was over 210,000 in 2009, for example, compared with 59,000 at Canary Wharf.

9. The concentration of business activity is unique. Offices make up 70% of all City floorspace, accommodating 80% of total City employment. The City does have a residential population but it is limited to about 10,000 residents who principally live within four estates concentrated around the edge of the City (at the Barbican, Golden Lane, Middlesex Street and Mansell Street), with smaller residential populations at Smithfield, the Temples, near to the River and at Fleet Street and Carter Lane. The core area of the City is focused on office and ancillary supporting activities.

10. The City's unique concentration of business activity and needs has been recognised in legislation governing the role of the Mayor of London in the determination of planning applications. The Town and Country Planning (Mayor of London) Order 2008, requires local planning authorities to consult the Mayor on planning applications deemed to be of 'potentially strategic importance'. The definition of PSI applications differs significantly in the City compared with the rest of London:

    - Development over 100,000 sq m total floorspace in the City, compared with 20,000 sq m elsewhere in central London;
    - Development over 150 m high in the City, compared with development over 30 m outside of the City.

THE VALUE OF THE CITY AS THE WORLD'S LEADING BUSINESS CLUSTER

11. The Government's Local Growth White Paper[1] suggests that locally driven solutions are the most appropriate way to support growth. It cites the key role of "agglomeration" effects in supporting growth in London (Paragraphs 1.14 and 1.15).

12. This is based on extensive academic economic research from the 1990s onwards which suggests that concentrations of economic activity in particular locations bring increasing economic returns, that is, £1 invested in an area which already has a strong business base in that particular sector, will create greater returns than in another location without that base or with a smaller base.[2] This is seen as the underpinning reason why major world cities like London have seen the strongest economic growth in recent decades.

13. This is linked to research into economic "clusters" defined as "a geographically proximate group of interconnected companies and associated institutions in a particular field, linked by commonalities and complementarities". These can operate at a range of geographical scales from city through to national level and beyond. Professor Michael Porter has identified clusters as one of the key drivers of competitiveness of regions and countries.[3]

14. The importance of business clusters has been recognised in National Planning Policy. Planning Policy Statement 4, Planning for Sustainable Economic Growth, states that authorities should ensure that the development plan "*Positively plans for the location, promotion and expansion of clusters or networks of knowledge driven or high technology industries.*" (Policy EC2.1c). This has been taken forward into the draft National Planning Policy Framework which also states that authorities should "*Positively plan for the location, promotion and expansion of clusters or networks of knowledge driven, creative or high technology industries*" (Para 73).

15. There is also recognition of the importance of specific clusters at the London scale, with the 2011 London Plan identifying the City of London as a *"strategically important, globally-orientated financial and business services cluster"* (Policy 2.10). London Plan Policy 4.3 promotes mixed use development, but recognizes (in Para 4.17) that *"Exceptions to this should only be permitted where mixed uses might compromise broader objectives, such as sustaining important clusters of business activity, for example in much of the City..."* The London Plan, therefore, promotes a flexible approach and the application of land use 'swaps and credits' whereby commercial development in the City makes a financial contribution towards the provision of affordable housing elsewhere in the City or beyond. This approach has been taken forward and reflected in the City's own LDF Core Strategy.

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[1] Local Growth: Realising every place's potential (2010), CM7961, HMSO
[2] Krugman, P (1991), Increasing Returns and Economic Geography, Journal of Political Economy, 1991, vol. 99, no. 3.
[3] Porter, M (1998), Clusters and Competition, New Agendas for Companies, Governments and Institutions, in On Competition (1998, Harvard Business Review.

16. The City of London is widely regarded as one of the best examples of a pure 'economic cluster' in the world. Its primary focus on financial services, with other businesses and land uses supporting that function, is one of its unique characteristics.

17. A detailed study into the issue was commissioned by the City of London Corporation. The report, *Financial Services Clustering and its Significance for London*[4], sets out a comprehensive evidence base on the nature of the London financial services cluster and policy guidelines to support the cluster. It identifies the benefits that the compactness of the City of London brings which include the promotion of personal relationships between key players and regular face to face interaction, the ability to serve overseas customers, and the density of information which supports knowledge flows.

18. The Greater London Authority has also undertaken research[5] into the economic benefits that agglomeration brings to the London economy. This includes a focus on the role of the Financial and Business Services sector in the City of London. It found that the City of London had the most specialised economic structure in the UK in 2001, a specialism that has been growing since the early 1980s, and where there is a positive, non-linear, relationship between employment density and productivity which in part accounts for high levels of productivity in the City of London.

19. This suggests that office and other business development in the City creates "*positive externalities*" which provide wider benefits to existing City businesses and to the London and the UK economy as a whole, and that these benefits would be higher than if this development happened in a different location.

20. This is not the case with residential development which would be likely to have similar economic impacts in other comparable areas of the Central Activities Zone, and probably greater multiplier effects in those other locations with more shops and services geared to a residential population. In addition, residential development in much of the City could have "negative externalities" through its impact on the efficiency and viability of office uses (see further below).

21. The research undertaken for the GLA suggests that if the agglomeration benefits of a particular location such as the City of London were reduced or damaged it would be likely to result in re-location to other major world cities with their own agglomeration benefits rather than elsewhere in the UK.

22. The "Local Growth White Paper" acknowledges that the main role for Government in the promotion of economic growth is in creating macro-economic stability and allowing markets to function efficiently and that local approaches to growth need to go with the grain of markets and reflect local circumstances. This echoes academic research

4 Financial Services Clustering and its significance for London (2003), Manchester Business School and Loughborough University for the Corporation of London

5 Working Paper 17: Why distance doesn't die: Agglomeration and its benefits (2006)

which suggests that it is very difficult to grow new clusters and that most have grown over time, independent from Government, where locational advantages exist.[6]

23. It is clear that the City of London has such locational advantages and one of these has been the direct focus on the needs of the financial services cluster through a long term, and evidence based, planning policy which restricts residential development. This brings major net benefits to the London and UK economies and supports the Government's wider aims for local and national growth.

THE AGREED NEED TO CONTROL RESIDENTIAL USE IN THE CITY

24. The unique characteristics of the City have developed as a result of decades of careful planning. A consistent approach has been taken through from the Local Plan which was prepared in the 1980s, the Unitary Development Plan which was prepared in the 1990s and, most recently in the Core Strategy.

25. The City of London Unitary Development Plan, for instance, was adopted in 2002 and provided:

"3.14 *The City is predominantly a centre of business and there are sites which are unsuitable for residential use. This could be because they are in locations where, for example, the surrounding activities and buildings, or disturbance from traffic would be harmful to residential amenities. Similarly, the introduction of housing into commercial areas may create expectations of residential amenity which, if met, would prejudice the operation of commercial activities or servicing, or constrain the form of future development. Certain sites may be suitable for large scale office developments, which the Corporation wants to promote, and piecemeal residential development on these would inhibit site assembly. In such cases, the corporation will refuse permission for residential development."*

26. This approach is supported by the GLA and was endorsed by the Planning Inspector who conducted the inquiry into the Unitary Development Plan. More recently, the City of London Core Strategy has been found sound at examination and adopted in September 2011. It does promote an increase in the residential population of the City but only from 9,700 in 2011 to 12,100 in 2026 and, again, with that growth being concentrated in the established residential areas on the fringe of the City. By comparison, the Strategy sets out plans to cater for an increase in employment of the City from 373,000 in 2011 to 428,000 in 2026. In order to achieve this the Strategy is clear that the City faces a significant challenge and, particularly, the need to continue to grow and renew itself to meet modern business requirements:

"3.1.1 *The City thrives on continued innovation in financial and business services leading to the early identification and development of new markets and investment opportunities. Innovation is facilitated by a concentration of business skills which gives the City of London an international competitive advantage. Providing additional office space will help strengthen this advantage.*"

[6] See Porter, pages 246 to 251, Government Policy at Cluster Level

27. In order to meet these requirements for change and growth, the Core Strategy plans the development of 1,150,000 sq m of additional office floorspace (Policy CS1). This will lead to an even greater concentration of office and commercial uses and, in order to help to achieve the necessary scale of new development, Core Strategy policy CS21 is clear that this must include "*refusing new housing where it would prejudice the primary business function of the City and the comprehensive redevelopment of large office sites.*"

28. This is a unique policy approach – it is not apparent in any other London borough or elsewhere in the country.

29. The Core Strategy was examined earlier in 2011 and the Inspector's report was published in June. The Inspector found that "*a mix of complementary uses supports the City's primary office function, the latter could be harmed by an inappropriate mix*" (paragraph 14 of the Inspector's report). Consequently, the Inspector directly endorsed the approach of the City in the following clear terms:

> "*The strategy is well justified by an extensive evidence base. It performs well in the Sustainability Appraisal, and it is in conformity with the London Plan and its Replacement. The predominant office function of the City, its crucial business role, and the long standing and successful policy of the Corporation to support these, means that the Core Strategy is right to reject other alternatives.*"

30. None of this means that the City is against residential development – just that it seeks to manage residential development to ensure that it does not take place in the wrong place, so that the location of housing does need to be controlled by the need for planning permission, in the unique circumstances of the City. The Core Strategy is planning to provide over 1,647 new residential units in the City during 2011-26, consistent with the London Plan's minimum annual target of 110 additional units.

31. The City also makes its contribution to meeting affordable housing needs. The Core Strategy requires new housing applications to provide 30% affordable housing on-site or 60% equivalent off-site with some flexibility to allow for scheme viability considerations. The Core Strategy also requires commercial developments including City offices to enter into planning obligations that normally allocate 30% of Section 106 contributions to the provision of affordable housing in or near the City. By such mechanisms the City Corporation has since 2000 provided approximately 500 affordable homes in neighbouring boroughs and 43 within the City. This has helped meet London's affordable housing needs without jeopardising the City's primary role as a business centre.

32. The City of London Corporation plays a direct part in meeting London's housing need by managing extensive affordable housing estates in inner London. It looks after more than 2,700 properties across six London boroughs - Hackney, Islington, Lambeth, Lewisham, Southwark and Tower Hamlets. It also has two housing estates - Golden Lane and Middlesex Street - within the Square Mile itself and manages the private residential Barbican Estate.

THE RISKS OF RELAXATION

33. The City needs to continue to renew and grow its office stock. The City has continued to renew its office stock over recent decades to ensure it continues to provide the scale and type of modern office accommodation needed by the international financial and business services sector. City office stock has increased from 75m sq ft in 1991 to 89m sq ft floorspace in 2011. Existing office stock in the City has a wide range of ages and ownerships and therefore there is always some redevelopment ‘churn’ as obsolescent stock is renewed. This contrasts with the Isle of Dogs where most current stock is in a single ownership and of a similar age that is not yet ready for replacement.

34. Analysis by leading agents Jones Lang LaSalle confirms that it is planning control rather than relative property value differences which have maintained the unique character of the City. At several times in economic cycles (including at the present time), residential values have matched and often exceeded office values, with the result that large proportions of the office stock in the City would be vulnerable to a free market in changes of use without planning control. This is particularly the case at times of financial crisis, when arguably the last thing that the City and its financial tenants need is competition for floorspace from a non-core use which could serve to dilute the concentration of office occupiers and inhibit the ability of the City to respond and to recover. A key element within the City’s Core Strategy, endorsed by the Planning Inspector, is the need to retain a strategic reserve of potential office sites, even during periods of downturn, to provide flexibility and a choice of high quality accommodation to potential future occupiers.

35. The most obvious impact of a relaxation of control, therefore, is a direct loss of floorspace from the City stock. Rather than planning for growth, the City would see a diminution in supply and a loss of critical mass. Jones Lang LaSalle has undertaken a separate review of those buildings in the City that have a lease event occurring over the next 5 years. They have taken only those events which relate whole buildings (i.e their assessment does not include buildings where only part of the building might become available). If assessed on viability alone, 13m sq ft, would be vulnerable to a change to residential use, based on comparative viability. The assessment excludes buildings under construction and large floorplate buildings as not being suitable. The proposed change to the Town and Country Planning (General Permitted Development) Order, therefore, would have a profound effect on the City.

36. An additional impact identified is that the loss of business floorspace to *res*idential use would have a significant effect on the net revenue achieved from business rates. Based on the average size of residential units consented over the last 10 years (68.6 sq m) and the top rate of Council Tax (Band H, £1878)) that is payable in the City (and using a gross to net ratio of 0.75), the rates/council tax that would be received for residential use equate to £3.39 per sq ft. This compares to business rates received for new / recently refurbished space in the region of £15 per sq ft. The impact of 1 million sq ft being taken out of office use would be in the region of £15 million compared to the new domestic rate that could be collected in its place of £3.39 million (assuming all are Band

H units). Given the scale of potential conversion identified by Jones Lang LaSalle, the implications for revenue to the public purse would be severe.

37. The implications are even more severe than that, however, because residential use brings with it certain rights and expectations which impact on its neighbours and their ability to operate as they need to.

38. One characteristic of residential use is that it tends to buy or lease for long periods. A residential demise will often benefit from a 99 year lease or longer, whereas office occupiers are normally subject to leases of 25 years or shorter. That lease cycle is important because it brings regular opportunities for vacant possession to effect refurbishments or even redevelopment. That dynamic helps to enable the City to continue to renew and reinvent itself to meet changing occupier requirements. The presence of one demise of a longer time period would prevent the achievement of vacant possession. The sporadic presence of just a few residential leases could undermine plans for large scale redevelopment.

39. The daylight and sunlight requirements of residential users differ from office tenants and can have significant impact on development in the City. Whilst it is acknowledged that national benchmarks cannot always be achieved in the densely built-up City, there have been instances where the existence of nearby residents has led to businesses not being able to secure the most appropriate accommodation for their occupation. A case in point related to a site on London Wall, adjacent to residential units, which was the chosen site for JP Morgan to house its consolidated European HQ building. Following extensive negotiations with the affected residents it became clear that the bank could not achieve sufficient space on the site due to the need to respect daylight and sunlight to adjacent residencies. As a result the bank could not meet its needs and was lost to the City.

40. Where residents exist careful analysis of the impact on daylight and sunlight needs to be undertaken. In many instances this has led to development not optimising the development opportunity of the site.

41. In addition, residential occupiers understandably expect a certain standard of amenity. The business function of the City, however, means that it operates 24 hours a day. Many businesses need to work to respond to international time zones but, importantly, the late evening, night and morning is the time when the City undertakes servicing, waste collection, cleaning and often construction – all of which create tensions with residential users. Constraints on servicing time (waste collection/street cleansing with machinery) are imposed around areas estates such as Barbican. This is becoming more widespread as the main residential clusters have increased in size or been complemented by new clusters (Carter Lane, Queens Quay/John Lyon House, Byward St/Tower Hill (Hotels) are all examples). Even new small scale residential concentrations can create an obligation to control servicing and working hours. The inclusion of residential uses at The Heron/Mansell Street has required restrictions to follow EU Directive hours of operation to prevent sleep disturbance (2300-0700). The problem is that the law on nuisance does

not require caveat emptor; there is a right to enjoyment of property, free from statutory and civil nuisance.

42. Real life recent examples in the City include:-

1. A small development of flats in a listed building opposite a major financial institution with a rear servicing yard opposite the flats. The impact of the flats is that the institution has severely restricted times that street works and deliveries can occur due to complaints about the impact of building servicing activities. There have also been a number of complaints regarding noise emanating from air conditioning units which has required the institution to insulate the plant enclosure at some cost to the business;
2. Flats above a shop adjacent to the City's tall building cluster have prevented 24 hour working on the tall buildings under construction which has resulted in an extended period of disruption for businesses and the general public due to the extended construction period which cannot be shortened by 24 hour working. This is currently impacting on the construction of the Pinnacle;
3. 20 Fenchurch Street is underway (Walkie Talkie) and the possibility of evening/night time work will become more difficult when residents occupy a small new residential development nearby in Brabant Court/Philpot Lane;
4. At Swiss Re (the Gherkin) contractors were prevented from undertaking night time work for most of the construction phase due to residents living in a conversion in Mitre Street/Creechurch Lane.

43. Once constructed and occupied, complaints can also arise from the ordinary use of office buildings. The City's Environmental Health team deals with complaints from residents arising from noise from servicing/infrastructure, maintenance, the operation of plant and equipment and licensing related activity, which can often lead to the need to impose constraints on activity and require works to be undertaken by the commercial occupier.

44. This level of friction, of course, arises from residential properties that have been allowed to develop through planning control, because the City does see value in providing for residential accommodation in the City. If residential uses are able to come forward across the City, however, in an uncontrolled way as a result of the relaxation of the Town and Country Planning (General Permitted Development) Order, the implications for the City's business occupiers and for its ability to develop the floorspace that those occupiers require could be severe. The City will have lost one of its most important unique selling points.

SUGGESTED AMENDMENTS TO THE REFORMS

45. The Government's consultation document "*Relaxation of Planning Rules for change of use from commercial to residential*" does acknowledge some of the risks inherent in the reform, including the impact on the supply of business premises and that it was not always the case that the new residential use would have less impact on its neighbours that the existing use (paragraphs 25 and 41). Consequently, the Consultation suggests that there may be a need for safeguards or for local authorities to put in place protections – which would potentially involve the use of Article 4 Directions, which would take away the general permission granted by the Government's relaxation. The difficulty with the use of Article 4 directions, however, is that:

    i) The imposition of a Direction would require a planning application to be submitted for the change of use. If the Government is not prepared to make an exception for the City in response to its representations, it is not obvious that the City would be able to resist individual applications against a background of national relaxation;
    ii) Even if planning consent was refused, the City of London would be liable to pay compensation for the loss. The potential losses could be significant in each case and that the number of applications could be substantial – it is unacceptable to expect the City of London to compensate applicants for the loss of speculative applications for proposals which planning policy has long sought to resist for sound planning reasons.

46. Accordingly, if the Relaxation is to go ahead, nationally, the City of London should be excluded. This would be easy to do within the Schedule to the revised Town and Country Planning (General Permitted Development) Order. For the reasons set out in this paper, the City's circumstances are unique and nationally important. No precedent would be set for other areas as there are no other areas with these special characteristics.

Topical Issues Papers are commissioned by the City of London Corporation to contribute to the debate on current issues and help the formulation of public policy. These papers are based on a review of existing evidence on different topics and offer an analysis of the options available.

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