From: Tony Crook
Sent: 10 March 2023 17:09
To: Housebuilding
Subject: Housebuilding Market Study

To whom it may concern

I am responding to some of the questions in your recently published consultation document and am appending to this email what I trust will be some useful papers for your reference.

My brief (but I hope helpful) response is to the specific questions you ask on planning obligations and affordable housing.

1. Re your para 2.39 (where you propose not to carry out further research on specific topics) you cite research done by myself and colleagues on the incidence value and delivery of planning obligations in 2018-19. You cite it as if MHCLG were the authors but it was commissioned from us by MHCLG and published by it. The key point is that this is the latest of a whole series we have done for MHCLG and its predecessors looking at incidence etc and the operation of S106 and CIL. With my colleague Professor Christine Whitehead (LSE) we also critically examined the objectives of land value capture via planning obligations and the difficulties of doing it in a prize winning paper published in *Town Planning Review* (appended as it also addresses the issues on which you seek evidence .see below)).

2. Qu 6 asks for evidence of differences within the UK. We recently completed a study for the Scottish Government. of the operation of planning obligations (S75 as they are known in Scotland). This was part of its evidence gathering for the intended introduction of its new Infrastructure Levy. (in statute but not yet implemented). We summarised the evidence in two recent papers in the journal *Town & Country Planning,* (the england/scotland comparison is appended) the first summarising the results and the second comparing England with Scotland. One key difference is that planning obligations continue to be combined with grants in Scotland to fund affordable homes with the results that far more social rented housing is secured in Scotland than in England (although land values are higher in Scotland as a result) . England via Homes England has a default of zero grant on S106 sites. (our scottish gvt report is at: https://www.gov.scot/publications/value-incidence-impact-developer-contributions-scotland/documents/

3. Qu 8c/d and Qu 17.. All our evidence in the many studies we have done shows that negotiations continue to be a key aspect of securing S106 agreements. Negotiations are particularly lengthy when local planning authorities have no local plans (half do not) or even supplementary planning documents covering S106 obligations. This makes it difficult for developers and also land promoters to price what to pay for land when negotiating with landowners. Hence the growing importance of options agreements to help them manage risk in the context of inadequate or absent policy. This Is even more acute when securing agreements become subject to conditions precedent once outline consent is granted. It also becomes more acute when planning authorities change their minds on what they require (or an upper tier authority eg a county in a two tier structure changes its requirements e.g. for school provision). There has notably been something of 'creep' during negotiations in recent years as many infrastructure provides turn to S106 in the context of their own capital limits (eg. the NHS). Evidence suggests that renegotiations have also become a more significant feature since the global financial crisis and market downturns, with affordable housing reductions being asked for (and often given) so as to secure the agreed contribution and/or funding for the required infrastructure . Importantly recent court judgments have indicated that local planning authorities are entitled to insist on provision originally agreed in negotiations in situations where developers may have paid over the market price to secure land in

the expectation that they can subsequently secure scaled back contributions and safeguard their margins on expensive land..Even if affordable housing is not 'sacrificed' in renegotiations it often results in more shared ownership provision than the social rented and/or affordable rented homes that local authorities prioritise.

4. Qu 9b. All our evidence gathered over several studies shows that negotiating S106 agreements is more difficult for SME builders than for larger volume house builders. The latter have the necessary expertise (including via consultants) and capital to conduct negotiations with local planning authorities (many of whom have less capacity and skills than applicants). Whilst SME builders may well have more local knowledge of site availability, they lack the ability, time and capital to engage in the extensive negotiations often necessary, although many of them are also operating 'below the radar' i.e. building on small sites that are not subject to S106 requirements, not the least in terms of affordable housing obligations.

5. Qu 10. Securing affordable housing via planning obligations is clearly not without difficulties but it is now a well embedded and understood policy in both England and Scotland.. Provided local authority policy is clear and is consistently followed, volume house builders (working through options agreements) can predict the costs of obligations and factor this into the price to be paid for land. It is less easy for SME builders but they too can make the system work when it has a reasonable degree of certainty. But where local plans have not been adopted and policy is uncertain this creates more risk for land promoters and developers, adding to the time and costs involved and it also creates more uncertainty for the local authorities as to what they can secure. Our evidence shows this risk is heightened where there is mission creep especially when other infrastructure providers (and upper tier local authorities) add more 'asks' to what is required and.this often leads to affordable housing being 'sacrificed' in negotiations. Market conditions are critical too so more can be and is delivered in southern England than elsewhere and less is delivered everywhere in market downturns. Above all everything is easier on greenfield than on brownfield sites. And when markets turn down developers will seek to renegotiate and it is often the affordable housing.element that is sacrificed by planning authorities as they wish to prioritise infrastructure . But in general our research has shown that in most cases most of what is agreed is delivered and where not it is largely because the development as a whole does not proceed..

Additional point. As you will know the Levelling Up and Regeneration Bill (now in committee stage in the Lords) proposes to introduce a new Infrastructure Levy, in effect a sales tax on the value of all completed developments originally intended to replace S106 and provide a much simpler approach to securing funding from developers for affordable housing and infrastructure and critically shifting more of the riks to planning authorities and away from developers. Now however the government plans to retain S106 for all site specific integral infrastructure and for all large and complex sites which will add rather than diminish complexity for both local authorities and developers. We did some early modelling of the levy (as initially proposed in the 2020 Planning Reform White Paper) and I have appended the paper we published. Colleagues and I have completed a study for DLUHC to model the proposals as they have emerged and I believe our report is shortly to be published by DLUHC. as part of its ongoing consultations on planning reform... This research has now been published by DLUHC and can be found at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1144482/Exploring_the_potential_effects_of_the_proposed_Infrastructure_Levy.pdf

Finally may I make it clear that my above remarks are my own and do not necessarily reflect the views of the colleagues I have worked with.

I am replying in my capacity as a chartered planner in academic practice and as someone who has done a great deal of research (with others) on planning obligations and at the same time has had extensive non-exec directorship in a wide range of housing and related organisations, including house building companies.. My main current non exec roles are listed under my signature (below). I am happy that any reference to this evidence is attributed to me by name. The evidence I have referred to above in answering your questions is all in the public domain specifically in the articles and papers I have appended to this email.

Please do not hesitate to get in touch with me if you wish me to clarify and/or enlarge this submission.

Yours faithfully

Prof Tony Crook

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Latest book and winner of 2016 RTPI Research Excellence Award:
'Planning Gain: Providing Infrastructure & Affordable Housing' by Tony Crook, John Henneberry & Christine Whitehead, published 2016 by Wiley-Blackwell

Latest article and winner of Sir Peter Hall award, 2020: 'Capturing development value, principles and practice: why is it so difficult?' Tony Crook & Christine Whitehead, *Town Planning Review*, 90(4), 2019, pp 359-381

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A. D. H. (Tony) Crook and Christine Whitehead

Capturing development value, principles and practice: why is it so difficult?

Land prices have risen significantly in England over the last two decades, generating debate about how far 'unearned increments', particularly those arising with planning permission, can and should be taxed for the public good. In principle, taxing such increases should be easy, although experience suggests otherwise. Taxing them, like any other tax, should be judged by how much is raised together with three welfare criteria: do they promote a more efficient use of resources; achieve more equitable outcomes; and comply with taxation principles of revenue raising, fairness and administrative competence. The paper discusses the two main UK mechanisms: unhypothecated national taxation and negotiated local contributions for infrastructure and affordable housing, assessing how far they have met these requirements. Finally, the paper considers how the current system might be modified better to achieve the desired outcomes and whether there is a case for more fundamental reform.

Keywords: land value capture, planning obligations, S106, Community Infrastructure Levy

Introduction

Land values have risen significantly in real terms in England over the last two decades (Figure 1), with much debate about taxing the resultant 'unearned increments' that accrue to landowners, something that has global importance as governments face increasing financial constraints and seek new sources of revenue (Calavita and Mallach, 2010; Ingram and Hong, 2012). The core concern is that, because these increments are unearned, often arising from public investment in infrastructure and planning permission, it is inequitable that landowners should take the benefits, and appropriate that government should, at the least, share them. This is reinforced by a general understanding that, in principle, such taxation does not reduce efficiency. Commentators regularly question why the current system of land value capture is inadequate and what could be done to generate a better approach (Aubrey, 2018; Barker, 2014; Civitas, 2018; House of Commons, Housing, Communities and Local Government Select Committee, 2018; Ryan-Collins et al., 2017; Shelter, 2017).

The UK's experience of directly capturing land value increases is mainly limited to two approaches: taxing development value (defined as the increase in land value that

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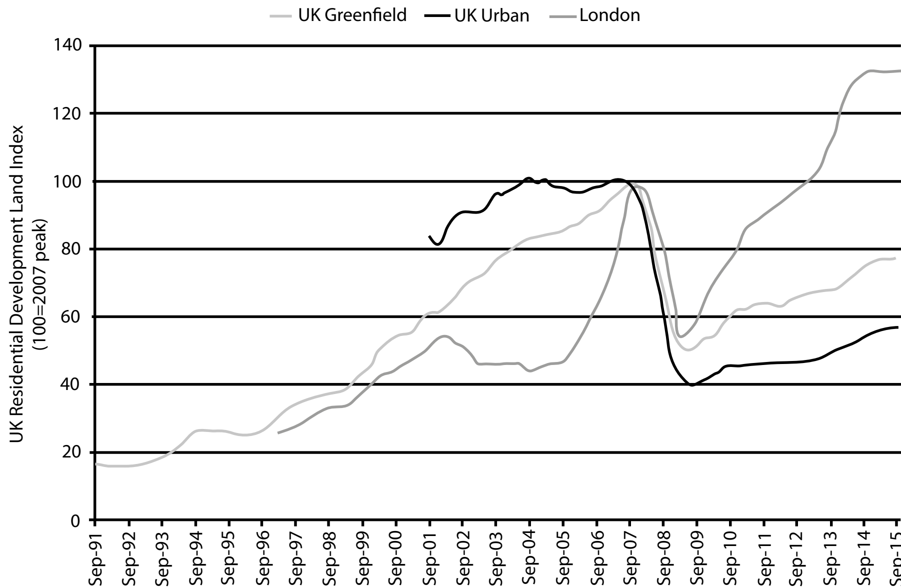

Figure 1 Residential Development Land Index, 1991–2015
Source: Redrawn from Savills Development Land Index

generally follows planning permission) through unhypothecated national taxation, and achieving similar objectives by negotiated local levies, including planning obligations and the Community Infrastructure Levy (CIL), funding local infrastructure and affordable housing (Crook et al., 2016). There have been no comparable mechanisms for taxing the increases that flow to existing developments from new infrastructure and other improvements and few for taxing the benefits that all landowners receive because of the impact of increased economic activity and general prosperity on land values.[1] There has thus been inconsistent tax treatment between land that is given planning permission and other land which benefits from increased land values but which is not taxed (Grant, 1992).

This paper addresses the question of what principles should underpin the taxation of development values, why what looks easy in principle has turned out to be so difficult in practice, and what might be done to ensure a more effective approach. First, it examines the causes of increases in land values, and in particular the role that development values play. It then goes on to discuss the criteria by which any measure of

1 There are more general taxes on transactions in assets as well as local business rates and Council Tax (discussed later). There is also no land-specific taxation of land values – as opposed to land value increases – but this issue lies outside our current remit.

taxation should be assessed: promoting greater efficiency in land allocation, achieving more equitable outcomes and complying with general tax principles. It then turns to practicalities. It examines the different ways development values have been taxed in the UK and how far national taxation and local levy approaches have matched the criteria earlier identified. The paper concludes by considering how to improve these instruments to generate more efficient and equitable outcomes – and whether they should be supplemented or replaced by more fundamental reforms covering all land value increases.

What causes increases in land and development values?

Land has no intrinsic monetary value: its value depends on its use. Land value is the residual from the income generated by the highest-value use of a site, less all the costs of generating that income, including required profit. A site's value is determined by competition between its various potential users. Its ultimate use is determined, subject to regulatory control, by the highest-value potential user. Development value is the increase in land value that arises from this development, compared with the existing value.

The land value of a particular site increases for several reasons. These include, on the demand side:

(a) changes in overall property and land values arising from increased economic activity and prosperity, generating additional demand for land and therefore higher land prices;
(b) increases in demand for land arising from the benefits of infrastructure investment broadly defined, e.g. greater accessibility and the resultant changes in opportunities and therefore, again, higher prices; and
(c) increased development values arising when planning consent enables higher-value opportunities to be realised from change of use, but also site-specific benefits resulting from (a) and (b) above.

If additional land could be readily provided to enable this increased demand to be realised, the effect on land values would be limited. The increases in land values therefore come from the incapacity of land with similar attributes, such as accessibility, to come forward at constant cost.

The supply of developable land is limited by these fundamental factors but also by other important constraints, notably planning regulations, which modify the potential use of land and the mix of dwelling types. Landowners also hold land off the market for owner-specific reasons and because they expect prices to rise further in the future. Taking all these factors into account, the lower the price elasticity of supply, the higher will be the development values.

Development values crystallise at the point when planning permission is granted. Planning permission enables a different, higher-valued use, which takes account of expectations of economic growth, the value of existing infrastructure and the probability of further relevant improvements, as well as the actual permission to change use. In the uncertain world of a discretionary planning system it may also be affected by the probability of adjustments to the planning permission itself.

Because of the way local authorities operate, the planning system varies and the land-price effects will similarly vary (Bramley, 2003; Cheshire et al., 2014; Evans, 2004; Gerald Eve, 1992; Hilber and Vermeulen, 2010; 2016; Monk et al., 1996; Monk and Whitehead, 1999; Whitehead and Monk, 2004). In particular, the tighter the constraints are drawn in areas of high demand for housing, the greater will be the development values arising from granting planning permission and thus the tax revenue that could be generated without affecting the use of the land.

How should we tax land value increases? Efficiency, equity and taxation principles

Land-taxation debates have a long history in planning, especially in the context of taxing development value arising from planning consent (Crook et al., 2016; Cullingworth, 1980). Debates have mainly concentrated on practical issues, including (i) how much development value is available to tax once the issues around valuation, incentives to make land available, interaction with other taxes, uncertainty around the economic environment and other factors are taken into account; (ii) how much it is acceptable to tax, given attitudes to 'unearned increments' and private property rights; and (iii) what the revenues might be used for if they are to be hypothecated for local infrastructure investment.

However, there are also issues of principle in that a good tax should be efficient, i.e. non-distortionary (not adversely affecting decisions about resource allocation); should be equitable between income groups or groups with other particular attributes, including between areas; and should raise revenues effectively and in line with tax principles of horizontal and vertical fairness and administrative simplicity.

Economic efficiency

Efficiency issues have rarely been debated, because the assumption is made that land taxation will not distort resource decisions as long as the tax lies within the development value envelope. However, broader-based analyses address the probability that there will always be alternative uses and thus distortions and that (i) good planning decisions and well-structured taxation can increase the social value of land and particularly reduce negative externalities arising from inappropriate land uses,

while (ii) poor decisions and taxes can increase costs or reduce values, generating inefficiencies.

The biggest issue with respect to the efficiency of land taxation is whether a tax will reduce land made available for development. The simplest models of land taxation (starting from Henry George, 1879) assume that land is homogeneous, that its total amount is fixed and that all land will be taxed at the same rate. If that is the case, the price of land is demand determined by the highest-valued use and any tax will simply have to be absorbed by the landowner. The same applies to taxing increases in land values.

However, this model bears no relation to the real world. As only a small part of total land is actually developed, more land can be made available as prices increase and land can be taken out of development if taxation makes it unprofitable. More importantly, land has very different attributes and therefore the highest-value productive use differs between plots – so planning and taxation will modify both the total amount of land made available and the allocation of land to different uses. In the context of taxing development value, it is imperative that the tax levied is less than the development value if distortions are not to be introduced. Given the many uncertainties associated with planning and development this may imply that the tax may have to be considerably less than the increase in value to limit efficiency loses (Crook et al., 2016).

Both planning and taxation can increase efficiency by dealing with land-market imperfections, including locational externalities; supporting the provision of public goods (like open space); improving information; and dealing with risk and conflicts between society and individual time preferences (Whitehead, 1984). However, poor planning decisions and ill-specified taxation can similarly worsen the situation, especially if proximate objectives are not in line with maximising social welfare.

Equity

In part because of the belief in the Henry George model, equity has often played a much larger role in debate than efficiency. Debates on equity underpinning public policy have tended to discuss either philosophical justifications for different conceptions of fairness or the practical consequences of these different conceptions for resource allocation (Wolff, 2008). Despite equity being central to planning objectives, planners have been more preoccupied with process than with distributional outcomes (Campbell, 2010; Fainstein 2010). Exceptions are planning debates about land taxation which have concentrated on the long-standing views that development value arises from 'no effort' on the part of landowners (i.e. 'unearned increment') and therefore 'should' be taxed; that such taxation would not reduce the supply of development land; and that tax would be easy to collect because land (unlike other assets and incomes) is fixed and cannot be hidden.

As an example of the equity argument, William Temple, Archbishop of Canterbury, suggested that property rights were a form of stewardship, subordinate to the general interest, and that 'there is no reason why we should pay certain citizens large sums of money for merely owning the land on which our cities are built (Temple, 1942, 117). Similarly, the wartime Uthwatt Committee (Ministry of Works and Planning, 1942) argued that planning control meant that those whose land got consent secured its development value whilst those whose land did not gain consent lost out and that this was inherently unfair.

As well as the 'unearned-increment' aspect of fairness, equity issues also arise when planning creates and enhances these values – e.g. when the supply of land is restricted, putting up the price of housing. Taxation can then compensate those who 'lose out' from planning policy by transferring assets from better-off landowners to poorer households, consistent with a Rawlsian approach to justice (Rawls, 1971). Importantly, Rawls argues that just outcomes need incentives for those who would help create them, suggesting that land value taxation should retain incentives for landowners and developers to sell land and carry out development.

Campbell and Marshall (2006) argued that liberal conceptions of justice, including Rawlsian, were too unrealistic because they ignored the institutional arrangements necessary to secure practical as well as just decisions. Hence we should spend our time looking for feasible possibilities, and not examining unavailable perfect solutions (Sen, 2009). To do this, Sandel (2009) endorsed a communitarian approach, i.e. one where citizens think together about what is fair in specific communities in particular places. From a planning perspective this suggests that decisions on capturing development values might be a matter for local communities as much as for national governments. Such an approach to equity is consistent with the empiricism and pragmatism that underpins policy in the UK (Gottlieb, 2016).

Taxation principles

Taxation principles themselves relate to efficiency and equity (both vertical and horizontal), but also to effective revenue raising, administrative ease and competence. In this context, the authoritative Mirrlees review of taxation argued that taxes should raise the required revenue, whilst avoiding 'inevitable' welfare- and efficiency-reducing side effects (Mirrlees et al., 2011, 21). Policy should define liability in advance, meet legitimate expectations, be administratively simple and address equity, benefits and ability to pay (Smith, 2015). For these administrative reasons, land and property taxes are amongst the oldest, with the advantage that land is easy to define and impossible to hide, and its ownership is recorded – at least in most developed countries.

As Mirrlees et al. note, taxation, to the extent that it changes use, is inherently distortionary, but these distortions can, in some cases, be positive, e.g. when tax is

being used to secure a more efficient outcome, such as to correct an externality or to pay for public goods. In these cases, there is the potential to improve outcomes at the same time as increasing efficiency (Whitehead, 2017).

Hypothecation (spending receipts on predefined projects) is more controversial. Some argue that earmarking taxes for specific purposes is a discredited idea (Giles, 2018), even though it is now gaining support in the UK as a means of making tax increases more palatable and spending revenues more transparent. Hypothecation is generally opposed by taxation experts. Mirrlees thought it unlikely that the optimal amount to spend on a programme was matched by the optimal amount raised. Moreover, because tax income may be volatile, this creates risks for spending and it was thus unwise to make spending contingent on a specific link to tax (Mirrlees et al., 2011, Chapter 13).

In the context of equity, taxation design must also consider the distinction between formal and effective incidence because the real burden of the tax will often, for good or ill, fall on someone who is not the legal entity liable for the tax. In competitive markets, incidence will depend on the relative elasticities of supply and demand (Needham, 2000; Skaburskis, 1992; Smith, 2015; Whitehead in Crook et al., 2016). As a general proposition, where there are tight planning constraints so that supply is relatively inelastic and there is significant price sensitivity of demand for housing, the burden of land taxes will fall on landowners. On the other hand, where supply is more elastic than demand, taxes will fall on consumers more than on landowners and developers. Thus when a tax is introduced the side of the market with fewer alternatives is likely to bear more of the burden (Smith, 2015).

Capturing development value?

Since the 1947 Town and Country Planning Act, the UK system of land-specific taxation has been based on capturing part or all of the increase in land value at the time that planning permission is granted. The increase in value takes account of (i) the benefits specific to the development following from that planning permission, (ii) the benefits from both past and projected economic growth which will enhance this value and (iii) existing infrastructure and expectations about future infrastructure investment or other improvements affecting the profitability of the development.

There are four distinct issues to be addressed when trying to capture development value.

(i) How should increases be captured through taxation?

The main approaches which the UK has used at different times include:

- Taxing the increased value within the national tax framework at rates that reflect both political attitudes to 'unearned increments' and the practicalities of

correctly assessing the added value and the incentives necessary for landowners to bring their land forward for development.

- A related approach, where the public sector purchases land at or near existing use value, undertakes or enables the investment necessary for development to take place and captures the resultant development value simply as a result of land ownership.
- A very different approach that gives local planning authorities powers to make charges that can be used to mitigate the adverse direct impacts of development where there is a 'rational nexus' between the development and these impacts. The revenues must be used to provide local infrastructure to offset these impacts. Over time this has been extended to include investment making the development acceptable 'in planning terms' without making the development itself non-viable.
- Latterly, enabling authorities to levy tariffs at local or regional level to fund necessary infrastructure both to mitigate the negative impacts of development and enhance future economic growth and community welfare.

These approaches are based on four quite different rationales:

(i) the first is, at least in principle, based simply on the view that 'unearned increments' should be taxed;

(ii) the second also reduces unearned increments but through change in ownership, but in addition hypothecates funds for infrastructure investment;

(iii) the third addresses the impact on local communities of new development, initially narrowly defined in terms of immediate costs but over time including much wider-ranging investments that help make the decision more acceptable in planning terms; and

(iv) the fourth provides an opportunity to raise revenues to pay for capital investments which will benefit a broader constituency including landowners (through increases to their land values), households and indeed all economic activity in the area affected.

(ii) Who should benefit from the value captured?

Past national land taxes have simply been treated as general tax income, so benefit the population as a whole. The second approach whereby public bodies buy development land net of the national tax and keep the incremental values benefits the acquiring agency and localities where the proceeds are spent. The third and fourth approaches,

where land value is captured in cash or in kind through planning obligations or tariffs, generate benefits for the immediate locality and/or the wider community, including compensating those who are adversely affected by development and providing infrastructure to specific groups, the community or indeed region more widely.

(iii) How to value what is to be captured?

Here the flexible and discretionary nature of the English planning system is important and contrasts with the zoning system in other countries where changing plans tend to determine changing land values (Booth, 2003). In England plans indicate but do not prescribe, enabling planning authorities to respond to changing circumstances. Thus there is considerable uncertainty about what might be permitted – and hence what the development value might be. Once full permission is granted the development value crystallises and can therefore be effectively taxed. Even so there is always the possibility that some of the increases in value arising from the permission may have been foreseen and therefore built into the pre-permission value, resulting in an undervaluation of development value. Remaining uncertainties may limit what people are prepared to pay and therefore reduce the measured development value.

(iv) How do other taxes affect development value tax?

There are other taxes levied on landowners which affect their overall rate of return and therefore what development value is available to tax. Capital gains tax and stamp duty land tax are levied on all capital transactions, including land and property. These will only be immediately relevant if the development or land is to be sold on but their existence affects measured values. Local annual taxation, in the form of business rates and Council Tax, also impacts on returns. In the case of Council Tax, the relationship of the tax base to increases in value is extremely limited, while in the case of business activity, increases are in principle captured through changing valuations and therefore higher tax levels.

Taxing development values and outcomes in England

Our detailed evidence on the incidence of and revenue raised by development-value taxes can be found mainly in Crook et al. (2016) and in Lord et al. (2018). Our submissions to a House of Commons Select Committee (Crook et al., 2018a; 2018b) summarised this evidence and drew out implications for policy based on this paper. Updating this section has enabled us to bring in additional material, including new evidence published in this volume.

National taxation

Table 1 Value of tax raised by national schemes and value of planning obligations

Development Value Tax	Year	Value, nominal	Value @ 2007–2008 prices	New homes completed p.a. by private developers	Value per house completed @ 2007–2008 prices
Development Charge	1952	£8m	£172m	36,670 (UK)	£4,690
Betterment Tax	1969–1970	£32m	£356m	185,970 (UK)	£1,914
Development Land Tax	1983–1984	£68m	£147m	153,020 (UK)	£960
Planning obligations – cash and in kind	2003–2004	£1,900m	£2,103m	130,100 (England)	£16,164
Planning obligations – cash and in kind	2005–2006	£3,927m	£4,163m	144,940 (England)	£28,722
Planning obligations – cash and in kind	2007–2008	£4,874m	£4,874m	147,170 (England)	£32,616
Planning obligations – cash and in kind	2011–2012	£3,700m	£3,400m	89,120 (England)	£38,151
Planning obligations and CIL – cash and in kind	2016–2017	£5,969m	£4,738m	121,000 (England)	£39,157

Source: Crook et al. (2016); Lord et al. (2017)

There have been three formal attempts directly to capture development value through national taxation. These all taxed development value, with the revenues going almost entirely to the public purse. There was related legislation on compulsory purchase and compensation. All attempts were implemented by Labour governments and all were repealed relatively quickly. Importantly, as Table 1 shows, they all raised very little money. All three schemes kept land off the market and there was limited public acquisition to counter this, let alone the capacity to land bank to help shape future development patterns.

The lack of success arose from five main factors:

- the geographically invariant and high national taxes deterred landowners from bringing land forward;
- there were problems assessing development value and ensuring liabilities were paid;
- developers structured developments to minimise liabilities;
- public land acquisition was required to comply with local plans but because these were out of date, these powers could not be used to build up land banks and counter land withholding; and
- landowners held on to land because opposition parties were committed to repealing the tax if returned to government.

However, there were two instances where development value was successfully collected, based not on taxation but on land ownership. First, post-war new-town development corporations were able to acquire land at close to existing use value (Cullingworth, 1979), enabling them to provide infrastructure, build affordable rented housing and make surpluses from land trading when selling land on to private developers. Second, similar arrangements were available to local authorities when acquiring land compulsorily in town centre comprehensive development areas where plans had been formally adopted. In both instances compensation reverted to full market value when national development value taxes were abolished (Crook, 2018).

Planning obligations

The idea of using the planning system, rather than taxation, to capture development value through requiring developers to pay for the infrastructure costs of their developments was originally initiated by local planning authorities. However, it became an increasing part of central government policy after the late 1980s. Formal national legislation was consolidated in Section 106 of the Town and Country Planning Act 1990. This allowed local planning authorities to negotiate obligations in the form of contributions from developers (in cash and kind) towards the infrastructure and community facilities needed to support new development. These are implemented through enforceable private contracts between planning authorities and developers. Contributions had to be justified on a 'rational nexus basis', i.e. the new development must 'cause' the need for specific infrastructure and the obligations must be related in scale and type to the proposed development. As well as securing infrastructure they also make proposed developments acceptable in planning terms, such as the provision of affordable housing. Since 2010 local planning authorities have also had powers to implement a Community Infrastructure Levy (CIL) as a fixed charge on all types of development with the intention that every type of development contributes

to the funding of sub-regional infrastructure. When CIL was introduced, planning obligations were restricted to site-specific infrastructure (widely defined) and affordable housing. CIL takes precedence over Section 106, so affordable housing may be squeezed out. Also, unlike obligations, there is no contractual link between charges and specific infrastructure projects.

Table 1 shows that planning obligations, in contrast to national taxation measures, have proved relatively successful in raising cash and in-kind contributions. The majority have been secured in London and south-east England, a reflection of the geographical pattern of land values, as well as of development. Obligations are largely delivered, with non-delivery arising mainly from changes to proposed developments or schemes not proceeding at all.

As long as developers fund contributions by paying less for land, obligations become a de facto tax on development value borne by the landowner, locally negotiated and 'hypothecated' for local needs – in effect a hybrid charge and tax. If this is the case, obligations should have no negative impact and would generally be regarded as improving on efficiency and equity. In practice, however, there will be some impact on what comes forward and what is built (for example, smaller homes at higher densities) – so there are efficiency distortions.

Landowners generally pay a higher proportion when planning authorities' obligations policies are clearly set out in their local plans and consistently implemented, and when national developers are seeking consent and acquiring land under options agreements. When authorities' policies are less clear, or when more inexperienced and often smaller builders are involved, the outcome may be different. When grant funding for the affordable-housing element is available, housing associations may pay higher prices for affordable homes built by developers (compared with a zero-grant position), so that higher land prices result and the de facto tax is reduced. Who pays then depends on negotiations over contributions. All these complexities mean that the proportion of 'available' development value that is finally captured, and therefore the amount the landowner is 'taxed', is extremely varied. We estimate that planning obligations plus national transactions taxes take on average perhaps a half of greenfield sites' open market values unfettered by obligations (Crook et al., 2018a).

There are five reasons why obligations have succeeded better than earlier approaches:

- unlike national taxes, obligations started as a 'bottom-up' policy led by local authorities, although later endorsed by national policy;
- the English courts have permitted a wide range of obligations provided they make proposed developments acceptable in planning terms;
- obligations are negotiated on a site-by-site basis, allowing specifics of the site and of its impact to be taken into account when negotiating land prices and determining viability;

- obligations have the character of a hypothecated tax because contributions are spent locally; and
- because obligations are enforceable private contracts, local authorities have confidence in developers delivering them and developers have confidence that the infrastructure they pay for will be delivered.

As we noted in our evidence to the House of Commons Select Committee (Crook et al., 2018b), which we based on our continuing research, planning obligations have at least four significant limitations.

First, they are dependent on the market. When market conditions are positive developers are keen to offer obligations to speed up consent; when market conditions worsen they either abandon developments or try to renegotiate obligations downward. After the global financial crisis there were concerns about sites being stalled, in part because of onerous obligations. In 2013 developers were given rights to seek renegotiation earlier than hitherto. The evidence (McAllister et al., 2016; University of Reading et al., 2014) suggested many reasons for developers taking up this right, some of which were the result of already negotiated obligations making projects unviable while others related to falling land costs which affected their balance sheets or simply the fact that new right made it easier to renegotiate contributions.

Second, the system can generate perverse incentives to planners, in that if they impose greater constraints on land supply, potential contributions increase. Equally, the authority may choose to enable higher densities, generating higher land values and potential contributions, benefiting both the authority and the developer, but also sometimes socially undesirable outcomes.

Third, negotiations take time and there is often a good deal of asymmetry in the skills and capacities between planning authorities and developers, resulting in slow negotiations and uncertain outcomes (McAllister et al., 2016). Partly to address this, many planning authorities have introduced some tariff-like fixed standard charges (e.g. a charge per square metre of floor space towards open space).

Fourth, whilst most large residential sites have agreed obligations, this is not the case for smaller sites or for commercial sites where, except for large retail developments, few have agreements. This partial coverage distorts what is developed. Equally, the fact that permitted development (such as the conversion of offices to housing) is not subject to obligations distorts the development mix and reduces the amount of affordable housing achievable.

Other limitations arise from the wide variations in planning authorities' obligations policies and practice (creating uncertainty for developers operating across authorities). These variations appear to arise from differences in the culture and behaviour of planning authorities and are not strongly related to market circumstances or indeed local needs (Crook et al., 2016; Dunning et al., 2019). This suggests that more could be negotiated and delivered within a more consistent framework. Reliance on flawed

residual valuation models to evaluate viability, especially in relation to 'benchmark land values', also appears to have reduced what is achieved through obligations compared with using more robust models (Coleman et al., 2012; Crosby et al., 2013; Henneberry in Crook et al., 2016; McAllister, 2019).

The 2014 revisions to the National Planning Policy Framework (which stressed that negotiated planning obligations should not undermine viability) appear to have led to developers especially in London paying land prices which cannot be sustained given the required obligations and then seeking to reduce the affordable-housing element. Successful renegotiations have then reinforced their preparedness to offer more for the land (Sayce et al., 2017). The recent High Court decision on the Parkhurst development in Islington (which stated that overpayment in relation to local-plan requirements could not be a reason for downward renegotiation) could well be an important judgment helping to reverse this behaviour (see also Crosby, 2019).[2]

Community Infrastructure Levy (CIL)

CIL has added new complexities. It has been adopted mainly by planning authorities in high-demand areas, especially London. In low-demand areas, viability concerns mean it has rarely been adopted, in part because the fixed charge can reduce the development value 'left over' for affordable housing, which continues to be a priority for many authorities. Because of this patchwork of adopting and non-adopting authorities, many small developments in the latter authorities are making no contributions to infrastructure even though they could afford to do so. And where it has been adopted it has proved more complex, uncertain and time-consuming than first anticipated. Also, significant exemptions have been introduced, reducing the proportion of development potentially contributing to CIL. For these and other reasons, less has been collected than initially anticipated (Community Infrastructure Levy Review Group, 2016; Lord et al., 2018; University of Reading et al., 2017). It is now also regarded as more uncertain than Section 106 because rates often change, and because CIL is a charge, not a contract, the timing or indeed the provision of the required infrastructure is unclear.

Matching experience to principles

Efficiency

The assumption of the simplest models, whether national or local, that there will be no negative impact on efficiency depends on there being no changes in development decisions made. In reality there are always both the possibility and incentives to change decisions about what is delivered and about bringing forward land for development.

2 *Parkhurst Road Ltd v. Secretary of State for Communities and Local Government and Another* [2018] EWHC 991 (Admin).

In the national tax context there are no incentives to reduce external costs (including congestion on consumer services) or other market failures or to provide public goods – it is just a tax.

Well-specified obligations, in contrast, can ensure that developers/owners pay the external costs and provide public goods (e.g. public open space) and so help secure more efficient land use. On the other hand, there may be considerable 'wastage' in what is provided and the resultant development may not be the most appropriate. Poorly specified obligations may lead to less development and particularly to fewer new homes overall, adversely impacting house prices, labour supply and productivity.

Equity

Equity through national taxation is achieved by taxing landowners on the 'unearned increment' and thus increasing overall government revenue. How and where these revenues are spent is entirely a matter for national government. Some of the costs may fall on other actors, notably developers and households and those who suffer from the negative effects of development but who are not compensated. Because higher tax rates reduce incentives to sell land, this may also breach Rawlsian principles of social justice, i.e. that those who produce the goods needed in a socially just society must have incentives to do so.

Planning obligations improve equity by reducing the 'unearned' income that the landowner receives for land. Obligations provide facilities for those directly affected by development, benefits accrue to the locality where the development value is created, and the adverse effects of new development on the local community can be mitigated through redistributing resources from landowners to consumers. The provision of affordable housing directly helps lower-income households. However, there may also be inequitable impacts in terms of who is actually helped by the obligations and who loses out. There are also issues arising from the complexity of the process, which may not just be inefficient but may also disadvantage particular groups, for instance small developers.

Revenue raising/taxation principles

Both taxes and obligations fail to match some principles. Land value taxes have a poor track record in raising revenue. Other increases in value arising from public investment are 'taxed' only if development related to this investment takes place (for example, the London mayoral CIL for Crossrail). Increases in value resulting from growing prosperity and economic activity are not taxed. The principle of horizontal equity is breached through exemptions, particularly with respect to small-scale development, and more generally where social costs are not recognised. The principle of

vertical equity is breached where levies fall on landowners with different capacities to pay, or when exceptions and exemptions are unrelated to that capacity. Finally, the principles of meeting legitimate expectations and being administratively simple have generally been breached in all these measures, often resulting in tax avoidance, long legal battles and high collection/compliance costs.

Overview

Planning obligations have secured far more revenue than national taxes. Unlike national taxation of development value, obligations' receipts are 'hypothecated' for planning-related local need and to offset costs to the community of the development. Contractual enforceability means that there is more certainty about what is delivered as long as the development takes place. Obligations have not been able to maximise potential revenue partly because many local authorities do not use the powers as effectively as they could and because there is a great deal of wastage in the process. Where they are used, viability negotiations may limit the take because of both inherent uncertainty and the relative power between authorities and developers.

While national land value taxes can in principle be efficient they have clearly distorted decisions in particular by holding land off the market or changing the timing of development. Obligations can also be used efficiently if they lie within (probably well within) the development value arising from planning permission. However, there is clear evidence of inefficiencies in that they modify decisions particularly in relation to density and dwelling type and tenure, as well as affecting viability.

Obligations breach 'horizontal equity' as not all benefiting from planning consents contribute (e.g. small sites) and not all affected by development are compensated by the provision of new local infrastructure. Although CIL was an attempt to ensure that all development contributed, the many exceptions and exemptions undermine potential horizontal equity. Because policies and practices are a discretionary matter for each local planning authority, there are big variations in outcomes between local authority areas with similar economic environments. There is also a broader structural issue that the amounts achievable relate to the extent of market demand. Areas with lower demand have fewer opportunities but may have similar or even greater needs.

As far as administrative transparency and simplicity are concerned the evidence with respect to national taxation is extremely negative – and supplemented by the fact that it was later felt infeasible even to introduce a Planning Gain Supplement, as proposed by Barker (Crook et al., 2016).

With respect to obligations, administrative transparency and simplicity have improved where good practice has been adopted; where policies are clearly specified in local plans; and where certain obligations are tariff-based, fostering predictability. However, negotiations are still complex, increasingly so on viability issues, and the

balance between planning authorities and developers remains asymmetric. And, despite good intentions, CIL has become complex and uncertain.

Moving forward

Are there better ways of capturing development values within the current system?

How can we improve the system? An important starting point is almost certainly incremental change by using and amending what works rather than starting from scratch (House of Commons, Housing, Communities and Local Government Select Committee, 2018; Travers and Whitehead, forthcoming).

There are a number of modifications already under discussion which could help promote more efficiency, equity and greater adherence to taxation principles. Although making viability judgements subject to plan policies, not according to the circumstances of each site (MHCLG, 2018b), risks deterring development if sites do not match plan-wide criteria, the recent Parkhurst judgment (see above) should secure more revenue and comply more with horizontal equity in taxation. Proposed changes (MHCLG, 2018a) allowing more pooling of planning-obligations revenue and permitting inter-authority CIL-like levies should improve efficiency by enabling more off-site infrastructure to be delivered. Other proposals may speed up processes and improve transparency but the decision not to remove exemptions to CIL will continue to limit what can be secured and breach the principle of horizontal equity.

There is a growing emphasis on large-scale development including 'mini' new towns/villages and urban extensions. The government has already introduced regulations to enable local-authority-led new-town development corporations (MHCLG, 2018c). The Letwin review (Letwin, 2018) goes further, proposing that all large sites identified in local plans be designated fully privately funded infrastructure development corporations. Their master plans would specify a diversity of housing tenures as well as (where viable) high proportions of affordable housing and infrastructure investment – so the land values in high-demand areas would be reduced very significantly (to a maximum of ten times existing use value). The general recommendation has been explicitly endorsed by the government, stating that housing diversification should be funded through reductions in residual land values (Secretary of State for MHCLG, 2019).

Although there is obvious merit in retaining the principle of negotiated planning obligations, securing greater revenues requires greater clarity of policy, increased speed of negotiation, and acceptance that more robust approaches need to be put in place to address viability issues in volatile markets. A core issue here is the central role to be played by the local plan in the effective delivery of development through generating a more certain environment for negotiation. The system might also include

thresholds (as are being used in London for affordable housing), giving those prepared to meet defined requirements speedier planning permission.

Although currently not favoured by government, a complementary reform would be to adopt the Peace review proposals for CIL (Community Infrastructure Levy Review Group, 2016) of putting in place a light, nationally determined, fixed tariff for all types of development, removing current exceptions and exemptions and generating revenue across the country. However, in lower-demand areas it might, even if kept low, negatively impact on development activity. A somewhat different approach, more in line with current government thinking (MHCLG, 2018a), would be to require that a CIL-like tariff be introduced in all authorities but with discretion to set rates in relation to the local economic environment – including a zero rate where absolutely necessary. To be effective, however, the current uncertainty problems associated with CIL (both rates and the timing of infrastructure investment) would have to be addressed. Negotiated planning obligations would still remain both to ensure affordable housing and for complex larger sites, particularly where the impact of the development extends outside the immediate neighbourhood of the development.

Many of these suggestions have been tried in London and their use continues to raise fundamental issues about the trade-off between raising funds and ensuring viability. Even in London, development value is not a never-ending stream to be used multiple times. Such over-optimism can rapidly reduce both developer and landowner incentives. In other regions the amount that can be raised, even with a much more effective collection mechanism, will often fall well short of what is required to support required infrastructure investment.

Broadening the tax base

The most important point to reiterate here is what we said about the current system in our introduction to this paper: that government has concentrated on the taxation of development value to the exclusion of other land and properties taxes that can capture increases in value arising from infrastructure and more generally from economic growth (Travers and Whitehead, forthcoming). The fact that taxation is concentrated on new development and indeed in particular regions distorts investment decisions and negatively impacts on innovation, productivity and future incomes.

Any broader-based reform would need to take into account the full range of property taxes now in place. In this context, OECD analysis suggests that the UK has the highest property tax take as a proportion of both GDP and total taxation. Moreover, around 50 per cent of the take comes from residential property and the tax on residential property is above the OECD average for *all* property taxation (OECD, 2018). However, a much higher proportion than in other countries goes directly to central government rather than to support local government expenditures as in most

other countries. Moreover, the system is highly distortionary at national level, in that taxes are only levied on transactions, capital gains tax is too easily avoided and stamp duty land tax significantly limits mobility and thus productivity.

The property tax system is particularly ineffective in the local context, because of exemptions which distort land-use choices and reduce revenues; a Council Tax system which is unresponsive to changes in either capital or rental values; and a business rating system which, while technically linked to rental values, suffers from irregular revaluations and assessments often poorly related to the rent actually paid (House of Commons Housing, Communities and Local Government Select Committee, 2019). Overall, the system is seen to be highly inefficient by theorists and practitioners alike (e.g. Mirrlees et al., 2011; IMF, 2018; House of Commons, Housing, Communities and Local Government Select Committee, 2018; Travers and Whitehead, forthcoming).

Measures that merit consideration include an annual land value or property tax which would be updated to include price increases associated with infrastructure and development as well as more general productivity increases – or it could be a tax solely on incremental increases (although then beware decreases). This type of tax is exemplified in Denmark, where it has historically proved reasonably successful (Kleven, 2014).

More in line with the overall approach to taxation in the UK would be (i) to modify capital gains tax to remove the exemption on primary residences and to make it less of a 'voluntary' tax – this would have the benefit of addressing all value uplift but only at the point of transaction; (ii) to heavily reduce or remove stamp duty, which is a highly distortionary tax on economic activity; and (iii) to reform the Council Tax system so that it better reflects capital values/rents and put in place mandatory updated valuations.

The current tax system provides a great deal of revenue to national government. If carefully structured, it could provide both higher and more responsive income streams for government at the same time as making it more equitable in relation to income and housing wealth. The benefits of shifting towards a much broader and more coherent tax base also significantly lie in improving efficiency and thus increasing productivity and growth. However, fundamental reform carries with it valuation, administrative and particularly political challenges which, as history has shown, make it difficult, if not impossible, to implement.

The planning obligation and local tariff route to taxing development values and hypothecating revenues to local and regional infrastructure has generally proved to be politically acceptable and relatively easy to modify and improve. While recognising that it is only part of the more fundamental story of how property can best be taxed, the case for maintaining a system which taxes these development values is strong, especially while it remains the case that the granting of planning permission provides such large unearned gains.

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funding affordable homes and new infrastructure – improving section 106 or moving to an infrastructure levy?

Tony Crook, John Henneberry and Christine Whitehead look at how the Infrastructure Levy proposed in the Planning White Paper is intended to work and how much it might be expected to raise; whether modifications might be needed if it is to meet the government's stated aims; and whether these aims could be achieved by simplifications to the current Section 106 and CIL arrangements

The proposed new Infrastructure Levy (hereafter the IL) aims to provide a much simpler way of capturing development value to help fund new affordable homes and the additional infrastructure required to support development. It does this by avoiding many of the complexities of the current Section 106 developer contributions and Community Infrastructure Levy (CIL) arrangements while including more types of new development – such as change of use and some permitted development (PD) – in the tax base as well as limiting exemptions to custom- and self-build homes.

In the debates and responses to the government's White Paper on planning reform in England[1] two main issues regarding the IL have been discussed:

- Will the IL raise more revenue than Section 106 and CIL, and will the money be available at the right times in the right places?
- Will it be possible to achieve the IL's objectives while maintaining its simplicity, or might it be easier to meet the same objectives by simplifying the current system?[2]

In the light of these debates, this article examines:

- how the IL is intended to work, how much it might be expected to raise, and where;
- what modifications to the IL might be necessary to meet its own objectives of simplicity and certainty in securing the funds required for infrastructure and new affordable housing and in addressing the regional 'levelling-up' agenda; and
- whether significant simplifications to the current Section 106 and CIL arrangements might achieve similar goals.

What sums might the IL raise?

How will the IL work?

The IL rate will be set nationally (although the White Paper recognises the possibility of central government setting different rates for each region and/or types of development), but the revenue will be collected and used locally. Mayoral/strategic

Duncan_Andison/Thinkstock

CIL in London and the combined authorities will become elements within the IL.

There is to be a threshold to the IL, based on average build costs per square metre and a small allowance for land value. Below the threshold, all developments will benefit from a zero tax. Importantly, unlike Section 106 and CIL, there will be no other exemptions from the IL, except for custom- and self-build homes.

The amount to be paid, while agreed in principle at the time of permission, will be charged on actual gross development value (GDV) at the point of occupation. This is the opposite of the position under Section106/CIL, where the value of the obligation (based on costs, not value) is fixed at the date that planning permission is granted. The change results in the risks posed by market volatility during the development period being shifted from the developer to the local authority. The local planning authority may borrow against the expected levy income in order to get the infrastructure in place – although this could be relatively expensive because of uncertainties about the value and timing of such income.

Subject to the requirements stated in the revised/simplified Local Plans, developers will be expected to provide on-site affordable homes, including the new 25% First Homes element of the affordable homes total. The net cost of the new affordable homes (defined as their market prices less the price paid for them by affordable providers) will be taken off the IL payment upon completion of the whole development.

How much will it raise?

Our understanding is that the government is not expecting the IL to raise vastly more than the existing system of Section 106 and CIL (although many commentators see that possibility as a major reason for change). Rather, it has promised that it will raise at least as much, including in terms of affordable housing numbers.

To address this issue we have used a residual cash flow model (examining all the income and costs of completing new development) to project the funds that the IL could yield if it were set at a fixed rate across the country. We have done this for a typical, 3 hectare greenfield residential development of 105 dwellings in each region of England.[3] The various assumptions that underpin the model are shown in Box 1 on the following page, but the core assumptions are that:

- average house prices and building costs for new dwellings are realised in each region;
- the IL is set at 20%;
- there is a requirement for 20% affordable housing provision (including First Homes); and
- the IL threshold is set at average construction costs plus a site value allowance of 10 times agricultural value.

Box 1

Core assumptions – prices, costs, thresholds, IL rates, and affordable housing requirements

Our assumptions use the most recent available data on new house prices, costs of construction, financing, and industry profits (for example, the Valuation Office Agency's land value estimates[A]). We have used a cash flow residual valuation model[B] to arrive at our estimates. Our core assumptions are:

- 105 new homes on a 3 hectare greenfield site – each home at 90 square metres with construction costs including the building of the homes plus fees, site development costs (assuming no abnormal ground conditions), marketing of the private homes, financing costs at 3.5% per annum (estimated over a 13-quarter development period), and profits at 15% of GDV.
- A sales price of £306,000 for the national estimate (approximate national average for newly built homes) with regional variations.
- An IL rate of 20%.
- No IL to be paid on sites with GDV below the threshold. For developments with values above the threshold there will be a zero rate on the amount up to the threshold. The White Paper suggests that the threshold will be related to construction costs and some contribution to land costs. We have assumed a threshold of national average construction costs and an allowance for land costs assumed to be ten times agricultural land value. Neither construction costs nor agricultural land values vary greatly by region, but house prices do.
- Other than as a result of the threshold there are no exemptions.
- An affordable housing requirement of 20% of the development, including 25% of this housing as First Homes, with the balance split between affordable rent and shared ownership.
- Housing associations pay 66% of market values for shared-ownership homes and 50% for affordable rented homes – these were the national average prices as estimated in our 2018-19 study of Section 106 and CIL for the Ministry of Housing, Communities and Local Government.[C]
- Developers sell First Homes at the required 30% discount on market price.

A *Land Value Estimates for Policy Appraisal 2019: Guidelines for Use*. Valuation Office Agency, Aug. 2020. **www.gov.uk/government/publications/land-value-estimates-for-policy-appraisal-2019/land-value-estimates-for-policy-appraisal-2019-guidelines-for-use**

B J Henneberry: 'Development viability'. In T Crook, J Henneberry and C Whitehead: Planning Gain: *Providing Infrastructure and Affordable Housing*. Wiley Blackwell, 2016, pp.115-39

C A Lord, R Dunning, M Buck, S Cantillon, G Burgess, T Crook, C Watkins and C Whitehead: *The Incidence, Value and Delivery of Planning Obligations in England in 2018-19*. Ministry of Housing, Communities and Local Government, Aug. 2020. **https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/907203/The_Value_and_Incidence_of_Developer_Contributions_in_England_201819.pdf**

The results for each region of England based on these starting assumptions are shown in Fig. 1 on the following page, together with the average for England as a whole. They show that most of the IL goes towards funding affordable housing, with less for infrastructure except in the southern regions of England; and that in two of the northern regions the IL produces negative land values.

We have also calculated the total yield from the IL for every region and aggregated it for England as a whole, using the total numbers of new homes completed in 2018-19 as the basis for grossing up; i.e. assuming that there are no exemptions for any tenures or development types. On this basis the IL yields around £5.6 billion in all, somewhat less than the £7 billion agreed for Section 106 and CIL in 2018-19. Then there were significant exemptions, especially with respect to small sites and permitted development (for Section 106), and little agreed for commercial development. In our modelling, just over 66% of IL is raised in London, the South East and East, only slightly higher than the equivalent proportion (64%) for Section 106 and CIL in 2018-19.

The main reason why the simple version of the national system generates less revenue is because, while the rate is national, market conditions vary greatly both between regions and between localities. Thus high-value areas can bear a higher proportionate tax than is being required, while in low-value areas the basic IL level cannot be achieved – as a result, developments end up either below the threshold or non-viable. A fixed-rate levy across the whole country (depending on the rate) could be expected to increase housing output in the South and reduce it in the North.

We have examined how the results are affected by assuming different thresholds (made up of different allowances for land values and construction costs), but these changes have little impact on the amounts achieved. The problem is not that these

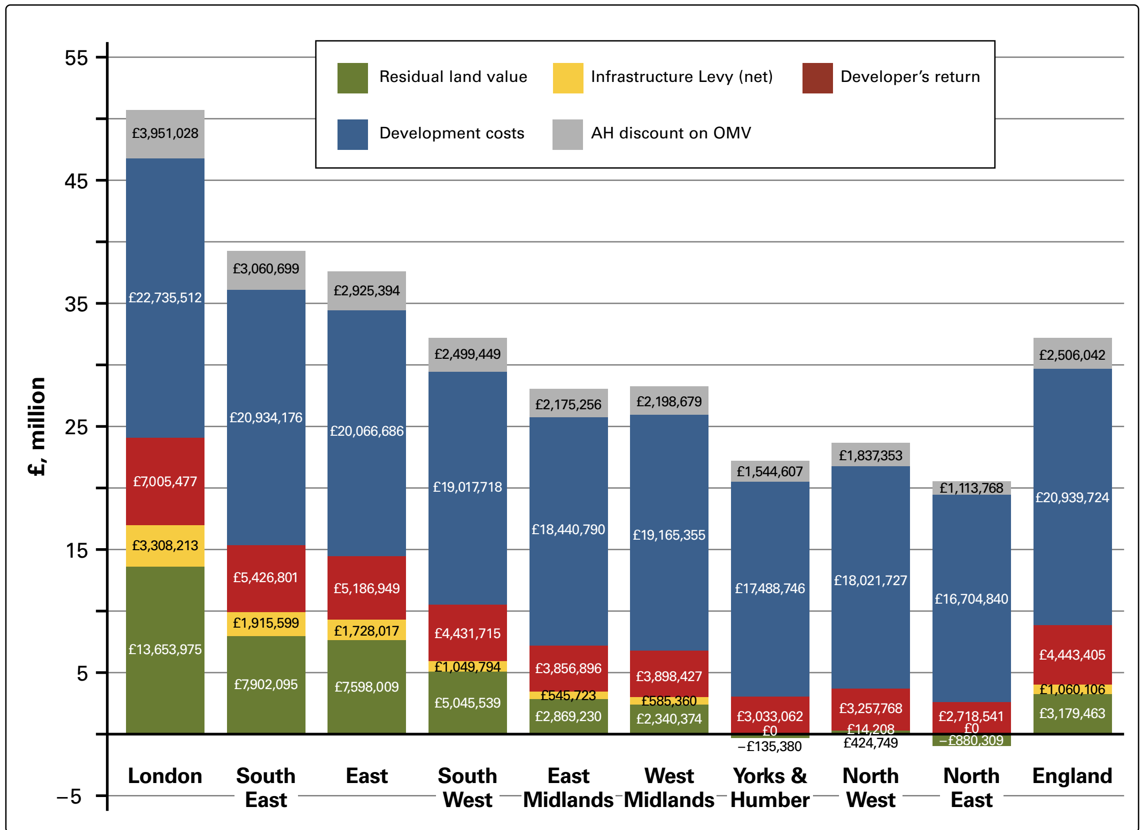

Fig. 1 Infrastructure Levy impact by region

costs vary but that values in some areas are inadequate. Only if the levy rate is raised and/or varied between regions (or local authority areas) can the revenues achieved be significantly increased.

Varying the rates

If the IL rate is raised to 30% (while leaving the requirement for affordable housing provision at 20%) it increases the total yield to £7.9 billion, somewhat more than Section 106 and CIL has been raising. But it further worsens the inter-regional stresses – with a higher proportion of the total (71%) being raised in London, the South East and the East and none being raised in the three northern regions, where there would be negative land values.

We also modelled the impact of levying regional rates to reduce the issues around viability on the one hand and funding loss on the other – but this inherently worsens the regional distribution. If, say, rates were 40% in London, 30% in the South East, the East and the South West, 20% in both the Midlands regions and 10% in the three northern regions, the IL would bring in £8.4 billion in total for England. However, none would come from the North East and very little (3% of the national total) would be raised in Yorkshire and Humberside and the North West, with £6.2 billion (74%) of the total being raised in London, the South East, and the East. What we cannot estimate is the impact of such an approach on output across regions, although we would expect some increase in the northern regions and some limited reduction in the South.

Taking both the fixed and regional versions, our model suggests that:

- On a like-for-like basis the IL would probably raise less revenue than that which has been raised by Section 106 and CIL, although the IL would be less complex and revenues more certain across the country.
- If, however, the wider set of planning reform proposals lead, as the government anticipates, to an increase in the numbers of new homes being built, the new IL has the capacity to raise more.
- The lack of widespread exemptions with respect to affordable housing and the better coverage of commercial development and change of use should also raise more, even if the total new build output does not increase.
- A simple national rate would work against the levelling-up agenda. The ways in which that issue might be addressed are by enabling variable regional levy rates or by requiring some of the sums raised in southern regions to be transferred to northern regions.

So is it worth changing the system – what is right and wrong with Section 106/CIL?

Significant sums have been raised by Section 106 and CIL. These increased by 170% in real terms from the £2.6 billion agreed in 2003-05 (at 2018-19 prices) to the £7 billion agreed in 2018-19. Within this total £2.3 billion was for infrastructure via either Section 106 (£1.3 billion) or CIL (£1 billion). The £4.7 billion for new affordable homes provided for 44,500 homes. Nearly half of all new affordable homes completed in 2018-19 were delivered by planning obligations on which no public subsidy in grant was paid.[4]

The success of Section 106, compared with previous nationally levied taxes on development values, is seen to be because obligations are a *de facto* and locally negotiated means of capturing development value that take account of specific site circumstances and values, as well as directly benefiting local people. Section 106 agreements have secured the confidence of local planning authorities because they are legal contracts that place obligations on both parties to deliver what has been agreed in a timely manner. They also give considerable certainty to developers that the infrastructure that is needed to complete their developments will be provided. We calculate that, because ultimately landowners pay the cost of these obligations, Section 106 and CIL capture about 30% of development value on greenfield sites, although there is usually less available on most brownfield sites.[3, 5-7]

Because Section 106 policy has emphasised on-site provision of affordable housing it has also contributed significantly to the mixed-communities agenda, with new occupants of market and affordable homes moving to the same new residential developments. These have tended to be in more 'upmarket' locations and have thus also enabled many deprived households (often with young children) to move to areas of lower deprivation.[8]

However, there are a lot of problems:

- Most importantly, local planning authorities feel that the negotiations not only hold up development but also that authorities are disadvantaged in negotiations as compared with developers – who undertake them all the time.
- Although there has been an increase in tariff-type charges in Section 106 policies, negotiations on Section 106 obligations are often drawn out, complex and uncertain, raising costs to both the local planning authority and the developer, as well as impacting on development viability.
- SME (small and medium-sized enterprise) developers find it particularly hard to engage with Section 106 requirements and negotiations, reducing the diversity of housing supply.
- Section 106 works less well in low-value areas and in times of stagnant or falling markets – and renegotiations can make everything slower and more expensive.
- There are big variations in outcomes between local planning authorities, partly as a result of local discretion in policy and practice – if good practice were more widely adopted, more could be raised.
- There are many exemptions in terms of both site thresholds and types of development (importantly, permitted development is exempted from Section 106), indicating that more could be raised were there to be fewer exemptions.
- CIL has 'de-linked' the contractual relationship between developers' payments and the provision of infrastructure; CIL money often sits in authorities' balance sheets for years. Regular changes in rates also add to uncertainties.

Will the IL overcome the limitations of planning contributions?

The proposed IL has the potential to overcome many of the limitations of Section 106 and CIL listed above. It will also allow the mixed-communities agenda to continue to be secured through on-site provision of new affordable homes.

Importantly, it removes the Section 106 negotiating complexities and many of the variations in local policy and practice. It will be a charge on all development – so is far more broadly based – and will be levied on the final value of completed developments (i.e. the GDV). Conceptually, the IL is a simple sales tax. This distinguishes it from Section 106 obligations that are designed to make development acceptable in planning terms by securing funds to cover the *costs* of infrastructure and affordable housing. As many of the lengthy timescales and risks that developers face under Section 106/CIL will be reduced under the IL, their cost of capital should be lower. This should make some additional development possible, as well as providing a more level playing field between larger and smaller builders.

What are the benefits and risks to developers and local authorities?

The IL, at least in principle, has an attractive simplicity and addresses many of the problems with Section 106 highlighted above. However, the details that will need to be decided suggest that the IL poses a different set of challenges. These include fixing thresholds, agreeing GDV valuations, determining the IL percentage, and dealing with the TIF (tax increment financing) style borrowing costs for local authorities that will reduce what the IL can fund.

Moreover, if market conditions change and the GDV differs from that projected at planning consent, there will be adjustment issues. If the GDV is lower, the government suggests that this might be dealt with by 'flipping' any on-site affordable homes into

the market sector. However this is likely to be problematic as affordable homes are generally the first to be built and sold to housing associations, helping developers' cash flow, and thus occupied by tenants well before the development is complete. If the GDV is higher, this will result in more income for the local authority, which may compensate for lower-than-expected incomes during market downturns.

In addition, the IL will shift the balance between certainty and risk both for local authorities and for developers. There are also suggestions that the IL income will not always be ring-fenced for infrastructure, affecting who in the community will actually benefit from the levy.

'While the IL has the potential to raise as much as Section 106 and CIL and address many of the problems of the current system, it will take time to introduce and 'bed in' the IL and to address its own problems – notably that it will not work well in the northern regions of England and the delivery of infrastructure is not contractual'

For local authorities there will no longer be the need for exhaustive analyses of the needs and costs for site mitigations and infrastructure to justify Section 106 policies on a site-by-site basis or wider CIL charge regimes (nor public inquiries into the same). If local authorities want IL to fund on-site affordable housing they will still need to have clear policies on this, but will be undertaking such analysis for their Local Plans anyway. IL income will depend on a range of factors, including levy rates and thresholds (and who will set them), valuations of GDV, and the changes in market prices that will occur between those estimated at planning consent and those achieved at the final sale of completed units (indeed, if they are completed). This will make the IL income to local authorities uncertain and will affect the costs of TIF-style up-front borrowing against that anticipated income.

For developers, large and small, certainty will increase. The complexities of negotiations will largely be eliminated (save for sharing their GDV estimates when applying for planning consent). They will know their liabilities well in advance, although these will not crystallise until completion, and they will not need to pay the IL charge until the development is finally completed. This will help with their cash flow. But one key aspect of risk will increase compared with Section 106. Developers will have no certainty that the infrastructure that their IL payments will nominally be funding will actually be delivered in a sufficiently timely manner to enable their development to proceed.

What is the best way forward?

While the IL has the potential to raise as much as Section 106 and CIL and address many of the problems of the current system, it will take time to introduce and 'bed in' the IL and to address its own problems – notably that it will not work well in the northern regions of England and the delivery of infrastructure is not contractual. The choice therefore is either to add some complexity to the IL so that it achieves its objectives as a simple value-based approach to contributing to the provision of infrastructure and affordable homes, or to simplify the existing Section 106/CIL system to achieve similar aims with less disruption but maintaining its cost-based approach.

There are ways of addressing some of the concerns about the IL, including:

- introducing regional IL rates, with the additional potential of having varying rates for different types of development or even rates specific to each local authority (or rates for sub-regions, for example the combined authorities) – this approach could include a standard minimum fixed rate across all regions, with regional or local 'top-ups';
- enabling infrastructure to be provided in kind by developers, which can be netted off from their IL liabilities, just as for affordable housing, although this will make both contractual arrangements and the valuation of such provision more complex; and
- addressing the levelling-up agenda by ring-fencing some of the IL yield in higher-value, mainly southern regions to help fund infrastructure in the lower-valued, generally more northern regions.

An alternative approach would be to secure the objectives of greater simplicity and certainty by amending the existing Section 106 and CIL system, including by:

- ensuring that the Local Plan is in place and clearly states infrastructure requirements, so there is much greater certainty on all sides;
- using a fixed tariff for smaller sites (say, up to 100 dwellings for residential and an equivalent for commercial) for affordable housing and site mitigation with no exemptions;
- retaining Section 106 for larger, more complex sites where discussions and negotiations are required for what is needed, whatever system is employed;

- for very large sites using a partnership-type approach, as suggested by the Letwin Review;[9]
- retaining CIL only for Mayoral CIL (London and combined authorities) for sub-regional/regional infrastructure; and
- incorporating CIL into the tariff, which should better link funding to requirements.

Conclusions

There is an attractive simplicity about the IL, although it will not be without complexities in its operation. There is also, as always, the challenges of introducing a new system. It is unlikely to secure as much as Section 106 and CIL currently do unless regional (and indeed intra-regional) variations in rates are used. It almost certainly cannot address the levelling-up agenda unless the government decides to redistribute at least part of the revenues – which has currently been ruled out. As it is envisaged in the White Paper, it cannot ensure that the necessary infrastructure is put in place in a timely manner.

We therefore argue that changes to what was initially outlined with respect to the value-based IL in the White Paper must be made if government objectives are to be achieved. We have suggested what some of these changes might be. An alternative would be to modify the existing cost-based arrangements to achieve similar objectives with less disruption. Based on the evidence, we leave the reader to decide which should be the preferred option.

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Notes

1 *Planning for the Future*. White Paper. Ministry of Housing, Communities and Local Government, Aug. 2020. www.gov.uk/government/consultations/planning-for-the-future

2 In addition, to simplify the IL further, some organisations have suggested removing the funding of new affordable homes from the proceeds of the levy to enable it to be used wholly for infrastructure funding (see, for example, *Written Evidence Submitted by the Royal Town Planning Institute*. FPS 113. Evidence submitted to the House of Commons Housing, Communities and Local Government Committee Inquiry into the Future of the Planning System. Royal Town Planning Institute, 2020. https://committees.parliament.uk/writtenevidence/13631/pdf/). However, while removing affordable homes from the IL might make it even simpler, doing so would raise key questions. How would affordable homes be funded in the future? How easy would it be for affordable housing providers to find suitable land to build on? What would such a change mean for the mixed-communities policy? Because of these uncertainties, other organisations want to retain the existing Section 106 arrangements (see, for example, *Written Evidence Submitted by the National Housing Federation*. FPS 158. Evidence submitted to the House of Commons Housing, Communities and Local Government Committee Inquiry into the Future of the Planning System. National Housing Federation, 2020. https://committees.parliament.uk/writtenevidence/15244/pdf/)

3 Projections of income from the proposed IL are set out in T Crook, J Henneberry and C Whitehead: *Additional Evidence Submitted by Professors Tony Crook, John Henneberry and Christine Whitehead*. FPS 164. Evidence submitted to the House of Commons Housing, Communities and Local Government Committee Inquiry into the Future of the Planning System. https://committees.parliament.uk/writtenevidence/18315/pdf/

4 A Lord, R Dunning, M Buck, S Cantillon, G Burgess, T Crook, C Watkins and C Whitehead: *The Incidence, Value and Delivery of Planning Obligations in England in 2018-19*. Ministry of Housing, Communities and Local Government, Aug. 2020. https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/907203/The_Value_and_Incidence_of_Developer_Contributions_in_England_201819.pdf

5 T Crook, J Henneberry and C Whitehead: *Planning Gain: Providing Infrastructure and Affordable Housing*. Wiley Blackwell, 2016

6 T Crook, J Henneberry and C Whitehead: *Written Evidence by Professor Tony Crook, Professor John Henneberry and Professor Christine Whitehead*. LVC 053. Second Memorandum of Evidence to House of Commons Housing, Communities and Local Government Committee Inquiry on Land Value Capture, Mar. 2018. http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/housin-communities-and-local-governmentcommittee/land-value-capture/written/79512.html

7 T Crook and CME Whitehead: 'Capturing development value, principles and practice: why is it so difficult?'. *Town Planning Review*, 2019, Vol. 90 (4), 359-81

8 T Crook, P Bibby, E Ferrari, S Monk, C Tang and C Whitehead: 'New housing association development and its potential to reduce concentrations of deprivation: an English case study'. *Urban Studies*, 2016, Vol. 53 (16), 3388-3404

9 O Letwin: *Independent Review of Build Out: Final Report*. Cm 9720. Letwin Review. Ministry of Housing, Communities and Local Government/HM Treasury, Oct. 2018. www.gov.uk/government/publications/independent-review-of-build-out-final-report

developer contributions for affordable homes and infrastructure — anglo-scottish comparisons and lessons

part two: scotland and england compared — a three-stage story?

In the second part of a two-part article on developer contributions for affordable housing and infrastructure in England and Scotland, **John Boyle**, **Tony Crook**, **Stefano Smith** and **Christine Whitehead** look at what the two countries can learn from each other to make the contribution systems work better, and they consider whether infrastructure levies are an appropriate way forward

Once upon a time—back in the early 20th century—developer contributions were a local prerogative in a world without the national planning systems that we have today. Local authorities could negotiate contributions with developers, usually for on-site mitigation purposes; transport and infrastructure investment were generally entirely separate decisions.

Until the late 1960s, local authorities in England needed central government approval before using contributions, but, after this requirement was removed, they started to see the potential for delivering affordable housing through the planning system, as well as the infrastructure needed to make developments acceptable in planning terms.[1] In Scotland, unlike in England, there was growing use

Both England and Scotland are seeking ways to use developer contributions to help to meet the regional infrastructure funding needs arising from development

of planning conditions, which required developers to provide site-related infrastructure before they could start work.

Evolution of the role of developer contributions

In England the big change came in 1990 with the Town and Country Planning Act. This consolidated the rules into what became known as Section 106 agreements, and planning policy introduced affordable housing as a material consideration, while formalising the requirement that contributions pass the rational nexus test. In Scotland similar rules were introduced in the 1997 Town and Country Planning (Scotland) Act.

At this point, the formal legal framework for what we are calling stage 1—enabling site-specific infrastructure and mitigation, together with affordable housing—was in place. The rationale for the approach was generally strong—requirements had to be clearly site related or there had to be an evidenced shortage of affordable homes. Thereafter, the policy became more embedded, and in both countries (despite complexities and concerns about the negotiation process) it was increasingly accepted by all parties.

The policy was framed as an instrument aimed at ensuring that developers would contribute to the costs of infrastructure and affordable homes. Who would actually pay was not part of the discussion, but, because developers generally address additional costs by paying less for land, developer contributions are actually a de facto means of capturing land value from landowners. This aspect has become more central to the debate, particularly because it implies that, as long as the development remains viable and the landowner is prepared to sell, there is no negative impact on output.

At this stage there was already a perceived need for what might be called stage 2—the capacity to require contributions to meet multiple-site, local and sub-regional infrastructure needs consequent on the development. Meeting these needs was seen as making the planning permission acceptable to the local community in planning terms.

Again, this was addressed initially by local authorities pushing the boundary. In England pooling contributions was enabled and, in 2010, the government introduced the Community Infrastructure Levy. This formalised an approach to enabling local authorities to raise funds for the broader infrastructure needs of the local area and its sub-region, directly related to the scale of development. Scotland, however, did not follow these approaches and so had to find other ways of taking account of these broader needs.

Now, at least in principle, we are entering stage 3—which, in both countries, addresses the question of whether and how developers can help to fund more wide-ranging regional infrastructure needs arising from development. The approaches to be employed are somewhat different (and still not entirely clear), but the problem to be addressed is the same: how to ensure that the infrastructure is put in place in a timely manner, and how to fund that infrastructure.

In this article, which follows on from our article in the preceding issue of *Town & Country Planning* surveying the story in Scotland in detail,[2] we examine each of the three stages—the first two in terms of the mechanisms actually employed, and the third by looking at what we know of the current proposals. We ask two questions: can the two countries learn from each other and so make the current systems work better; and are infrastructure levies an appropriate way forward?

The existing systems—learning from one another

Stage 1: Site-specific mitigation and affordable housing

Since the 1990s, developer contributions have made an increasing contribution to both site mitigation and affordable housing. Regular assessments in England and now in Scotland have shown growing numbers of agreements and higher contribution values.[1-4] Moreover, the approach has become increasingly accepted by all parties, despite concerns about complexity, the costs of negotiation, and issues of relative power.

Site mitigation

Site mitigation in both countries is designed to ensure that proposed developments are acceptable in planning terms and that developers contribute to the costs of any mitigation needed to make it so—for example contributions to the provision of off-site infrastructure such as local roads. In both countries such mitigation must be clearly related to the development in question.

In both countries this works reasonably well, provided that local development plans are clear, up to date, and followed through and implemented

consistently. Where they are not, especially where plans are out of date or not followed, developers have difficulty in estimating what to pay for land, and so they, rather than landowners, may end up paying part of these costs, which impacts on their preparedness to build. Many developers now seek to reduce these risks by using options agreements which defer land price agreements until all the contributions are agreed with local authorities. Even so, this adds to risk. In both countries site mitigation is more challenging on large and complex sites where there are several developers and lengthy build-out timescales over which market conditions and costs often change.

In Scotland, unlike in England, significant use is also made of planning conditions to secure site mitigations by requiring developers to ensure that specific infrastructure is provided before development can commence. How this is done and financed is a matter for developers, because conditions may not directly identify financial payments. The evidence from our research showed that the use of conditions in Scotland, where legally enabled, is accepted, well understood, and can help to speed up the provision of infrastructure and assist in getting development on permitted sites under way.[3]

In England, the range of contributions has continued to be extended to cover more general community infrastructure—which has sometimes been regarded as ‘mission creep’. This trend has been much less obvious in Scotland, where there has been more emphasis on maintaining the site-specific rules. Importantly, in Scotland, recent court and reporter decisions have further restricted this creep.[2]

Affordable homes

The central role of affordable housing in developer contributions, particularly on-site provision of that housing, formalised in planning policy before and after the 1990 and 1997 Acts, could be argued to be inconsistent with the principles of developer contributions, in that they are not a consequence of the specific development. Rather, it is enabled by an evidence-based assessment of the need for affordable housing identified in local development plans.

In both countries developer contributions contribute significantly to providing new affordable housing. In this way, landowners who get the benefit of planning consent contribute to the costs of providing new affordable homes, especially in areas of high house prices, where low-income households are often priced out of market homes. Significant amounts are secured and delivered through these contributions, although the amounts depend on having clear policies in adopted plans and implementing them consistently (and also, in Scotland, on having long-term partnerships between housing providers and private developers).

While acceptance of the approach is high in both England and Scotland, in England affordable housing numbers tend to be the first thing cut during negotiations over viability, especially on large sites with multiple developers and long build-out times and when market conditions change, to protect site and wider infrastructure contributions. In Scotland, partly because of the availability of grant, the provision of affordable housing in almost all schemes is sacrosanct in high-valued areas, notably Edinburgh. In areas where there is less land value available, there is often less room for manoeuvre.

Developer contributions have long played a major role in the provision of affordable housing

The biggest difference between the two countries is with respect to the types of homes provided. In England, there is considerable emphasis on shared ownership rather than rental units and on affordable rent rather than social rent. The dwellings are also generally quite small. A far bigger proportion of the total provided in Scotland is in the form of social rented homes. Moreover, the variety of sizes is greater and reflects local needs more directly.

An important reason for this difference is that, in Scotland, the availability of grants for affordable housing providers makes it possible to reduce the contributions required of developers (and thus also feeds through into higher land values). In England, on the other hand, there is a zero-grant default for new homes secured through planning obligations—although there are numerous exceptions.

Stage 2: Other community needs and non-site infrastructure

Not surprisingly, over the years there have been many pressures to extend the range of developer contributions as a means of funding necessary local infrastructure. Three distinct issues have been addressed to varying degrees:

- how to fund infrastructure which arises because of the cumulative effect of developments;
- the provision of infrastructure for community services which can be seen to be related to changes in demand arising from development in general; and
- the provision of broader-based sub-regional or even regional infrastructure.

Scotland has faced problems in dealing with the cumulative impact of small-scale developments, as, legally, resources cannot be pooled in this context. England, on the other hand, has addressed these issues by fixed tariffs and the legal capacity to pool contributions from a number of developments. Experience suggests that this type of problem is therefore reasonably easy to solve in ways consistent with general principles.

With respect to community services, developers have increasingly made contributions to education, wider transport services, open spaces, play and leisure facilities, and, increasingly, health facilities. Developers have concerns around 'scope creep' in what is required, which they see as impacting on viability and making it difficult to estimate appropriate land prices. Other requirements—such as obligations in England to secure biodiversity net gain on all developments needing planning permission—are raising similar concerns.

In Scotland, there has been some push-back, notably with respect to health facilities, which some developers think should be paid for by central government rather than by them. In Scotland, local authorities also face challenges in co-ordinating the spending of contributions where the infrastructure provider is outside the local authority, although less so where the provision is made by the local authority collecting and indeed spending the contribution.

Sub-regional and regional infrastructure

The principal problem facing both countries is that of securing contributions for infrastructure which is not directly related to mitigating the site-specific impact of new developments. How to secure contributions towards the wider infrastructure needed to support all new development, especially when this involves more than one local authority, is a major challenge. Indeed, the legal requirements that contributions exacted under Section 106 (England) and Section 75 (Scotland) agreements must be directly related to developments is often interpreted as preventing their use for broader infrastructure.

The funding problem was addressed in England through the introduction of the Community Infrastructure Levy (CIL). This enabled local authorities to secure funding for off-site infrastructure where the rational nexus did not apply. Developers were required to pay a charge based on net additional square metres provided, to be used to pay the costs of defined infrastructure programmes. A mayoral CIL in London was also set up to help fund Crossrail, and there are intentions to enable the mayors of combined authorities to introduce similar levies to fund cross-boundary infrastructure.

However, CIL has not been as successful as had been hoped, especially for large and complex sites. Many developments are exempted from the charges; and, in contradiction to the intent of CIL, some of the funding also has to be used for very local, parish level spending. Many authorities have not adopted a CIL on viability grounds, especially those wanting to protect affordable housing contributions in relatively weak markets.

Moving on to stage 3: Infrastructure levy approaches

Traditionally, larger-scale infrastructure was paid for by central government grants, but these are clearly limited. So it is not surprising that governments in both countries are seeking to find new sources of funding. Equally, it has been argued that there is plenty of potential for increasing developer contributions, which can still be paid for out of land value increases arising from granting planning permission. What is less clear is whether the rationale is still consistent with the original objectives of developer contributions or whether it is simply a land value tax by another name.

In this context, each country has proposed some more radical approaches based on introducing infrastructure levies, but each with rather different objectives—Scotland to address sub-regional infrastructure needs, and England to replace the existing Section 106 and CIL arrangements which are seen to cause delays and to be administratively burdensome.

Following commissioned research,[5] Scotland put a potential infrastructure levy on the statute book in 2019, although the government has yet to implement it. The intention now is to introduce legislation in 2023–24. The levy is intended to 'capture a proportion of land value uplift, so that there can be public benefit from the value created by planning decisions and public sector investment'.[6] The proposed levy would 'support the provision of infrastructure and services which will benefit and incentivise the delivery of development across a wider area, and help to unlock sites planned for development'.[6] It would be collected by local authorities and spent by them on a defined list of infrastructure which covers a wide range of potential needs, including community (for example schools and health) as well as other kinds of infrastructure (for example roads, water, energy, and flood prevention).

To date, no decision has been taken as to the form the levy would take—for example either as a contribution towards defined costs (such as CIL in England) or as a charge on the value of the development created (as proposed for the Infrastructure Levy in England).

England is also considering a mandatory Infrastructure Levy, not as an additional mechanism but rather as a replacement for Section 106 agreements and CIL as part of a broader planning reform (although the latter now looks unlikely to happen). The intention is to replace the cost-based contributions of Section 106 and CIL with a levy based on the sales value of developments.

The Infrastructure Levy in England would be collected only above a value threshold based on the costs of development and an allowance for some

land value.[7] It would replace the complexity and uncertainty of the current arrangements with a much simpler and more predictable approach and reduce the lengthy negotiations, which are seen as particularly problematic for SME (small and medium-sized enterprise) developers. The stated expectation is that this proposed system will raise at least as much funding as is currently delivered, including as many new affordable new homes, mostly still to be provided on site, as is the case under Section 106 agreements. Others see the potential for it to raise much more and become the equivalent of a quasi-hypothecated land value tax on new development.

The levy would be paid on the value of completed development when it is occupied. To ensure that the infrastructure necessary to make development acceptable in planning terms can be provided in a timely manner, local authorities will be able to borrow against anticipated revenues.

Although the simplicity and predictability of the proposed system is to be welcomed, it will not be without complexities. A preliminary assessment of the proposal, based upon modelling its impact on funds secured, showed that a national rate would be unlikely to achieve the government's objectives because it would either secure too little in southern England or (if it were to avoid this) it would make developments elsewhere unviable. Hence regional or sub-regional rates would be required.[8]

'An obvious three-pronged approach might distinguish different types of sites: smaller sites; larger, more complex sites; and major developments. This would primarily build on and develop existing developer contributions practice'

The government has subsequently indicated that it would give local authorities the power both to set rates (which would almost certainly have to vary within an authority) and to collect and spend levies. The hoped-for simplicity is therefore unlikely to be realised. While it may well prove simpler and less risky for developers (although they lose their contractual Section 106 right to ensure that their contributions are used for infrastructure), it is likely to prove riskier for local authorities, and deciding on local levy rates and threshold levels will be challenging. An obvious concern, with respect to current government policy, is that without a mechanism for redistribution between areas, the levy is likely to be inconsistent with the levelling-up agenda.

Looking forward — learning from experience in England and Scotland

The experience in both countries, as well as the current proposals for change, raise a number of issues about how developer contributions might be better handled. In particular, can raising developer contributions through a single approach covering all types and sizes of developments work, given the complex variety and range of sites and circumstances involved? Additionally, should the amounts secured be related to the costs of provision — a fundamental principle of the original developer contributions approach — or to the value of the development being created? This is a choice which raises the more fundamental question of whether these policies are now being designed explicitly to capture land value increases or to secure developer contributions to infrastructure costs (with land value capture being an outcome but not an explicit objective, as in earlier developer contribution policies).

Depending on final decisions we may have two different levy approaches. The levy in Scotland may proceed as a cost-based approach, despite policy stressing this as a means of land value capture — whereas the English levy, as proposed, is to proceed as a value-based approach unrelated to the costs of mitigations and infrastructure. Each country will doubtless want to see how these different approaches work in practice and if there are lessons to be learned.

Based on our research in both countries, an alternative approach could be to have systems that are appropriate to the types of sites involved, because each site (or at least each type of site in terms of characteristics) is different. Such an approach would still depend on local authorities having clear and regularly updated local development plans; carefully identifying sites for development within these plans, clarifying how each would be treated in terms of developer contributions; and further clarifying how 'windfall sites', not allocated in plans but brought forward by developers, would be treated.

An obvious three-pronged approach might distinguish different types of sites: smaller sites; larger, more complex sites; and major developments. This would primarily build on and develop existing developer contributions practice rather than putting in place completely fresh approaches, which inevitably take time to bed in and thus risk undermining the implementation of new development (at least for the time it takes for new practices to evolve).

For small sites with short build-out times, including those where on-site provision of new affordable homes is not sensible, one could envisage a simple tariff. This could be based on floorspace or numbers of homes to be paid by developers towards the costs of site mitigation and the extra community needs generated by such developments, which cumulatively can be substantial. In England, use could also be made of planning conditions to achieve new infrastructure, building on the experience of Scotland.

For larger sites, including those with long build-out times and perhaps multiple developers, something along the lines of negotiated contributions to the infrastructural and community needs generated by these developments over time would be more appropriate than a fixed tariff. Even so, there might be a case for indicative rates, allowing for changes as conditions, revenues and costs change over the construction period.

For major developments, such as new villages, significant urban extensions, or substantial urban regeneration sites, one could envisage more partnership types of approach, taking account of the models set out in the Letwin Review in England[9] and the masterplan consent areas now provided for in the Scotland Planning Act of 2019. These can involve several landowners and developers working in partnership and, within a clear developer contributions policy, set out what is required and shape the land value expectations of landowners whose land is to be acquired. The partnership would thus acquire land in a way that fully reflects the required contributions and realises the value inherent in the proposed new development when it is built out, helping to fund the infrastructure and community facilities needed.

Such an approach would be more acceptable than changes in compulsory purchase compensation that would mean only existing-use value would be paid to landowners whose land was acquired (as has often been proposed). Instead, clear policy on developer contributions would mean both partnership and private sites would get the same market value, one that had taken account of these required contributions.[10]

Conclusions

In both countries, there has been general acceptance by all parties of the principles of developer contributions for site mitigation, for community needs related to new development and for affordable housing provision; but there has also been acceptance that they cannot easily and effectively provide for infrastructure requirements needed for wider development. The reasons for introducing these new levies are not simply that levies might be better at raising funds than developer contributions, but that new approaches are needed not only to secure funding for non-site-specific infrastructure but also to ensure greater co-ordination, including the timing of all new infrastructure.

However, there are risks for both countries in introducing something brand new in terms of the proposed levies, which is why we suggest that there might be merit in thinking of adapting the existing systems. Introducing change within the current frameworks of policy and practice by clarifying, in particular, how they can simplify processes and be used for all three elements—site mitigation, community needs, and non-local infrastructure—might be less disruptive.

We also note that all new infrastructure, however funded, benefits existing residents and businesses, as well as the occupiers of the new developments. There is thus a much wider question as to whether we need better mechanisms than our existing land and property taxation framework to ensure that they too pay for these benefits.

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Notes

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