Gathering the windfall

How changing land law can unlock England's housing supply potential

Working Paper 03/2018

September 2018

centre for **progressive policy**

Thomas Aubrey

Centre for Progressive Policy

About the Centre for Progressive Policy

The Centre for Progressive Policy is a new think tank committed to making inclusive economic growth a reality. By working with national and local partners, our aim is to devise effective, pragmatic policy solutions to drive productivity and shared prosperity in the UK.

Inclusive growth is one of the most urgent questions facing advanced economies where stagnant real wages are squeezing living standards and wealth is increasingly concentrated. The Centre believes that a new approach to growth is needed, harnessing the best of central and local government to shape the national economic environment and build on the assets and opportunities of place.

Centre for Progressive Policy
27 Great Peter Street
London SW1P 3LN

+44 (0)20 7070 3360
www.progressive-policy.net

Executive summary

Over the last few years there has been a growing cross-party consensus that to raise the rate of housebuilding, England needs to increase its investment in infrastructure, thereby opening up land for more homes. There is also a growing consensus that a greater share of the uplift in land value resulting from planning permission awards should help fund incremental infrastructure investment including affordable housing.

Infrastructure investment on vacant and derelict land enables more homes, including more affordable homes, to be built that are connected to jobs, while ensuring access to schools and hospitals. The challenge is that providing infrastructure for larger developments is costly which is why the increase in land values as a result of planning permission awards needs to play a greater role in funding these kinds of projects.

The awarding of planning permission dramatically increased average agricultural land values from £22,520 per hectare to £6.2m per hectare for average residential values for new builds in 2016/17 across England; an increase of more than 275 times.

Analysis by the Centre for Progressive Policy (CPP) based on recent Ministry of Housing, Communities and Local Government (MHCLG) figures indicates:

Pre-tax windfall profits of **£13.4bn in 2016/17** were generated as a result of land being granted planning permission. By contrast, only £5bn was captured directly from the uplift in land values or 27% of the total uplift.

Residential land values for newly built homes **increased by 50% from £14.8bn to £21.5bn** between 2014/15 and 2016/17 due to a combination of increased output and rising land values.

Assuming that all tax receipts are collected on these windfall profits, up to an additional £2.8bn could be generated for central government. This implies the post-tax windfall profit for landowners and other stakeholders as a result of land being granted planning permission is **£10.7bn for 2016/17**. If this windfall were redirected to help fund infrastructure investment and affordable housing, then up to an **additional £214bn would be available over the next 20 years.**

Assuming similar tax levels for 2014/15 and 2016/17, windfall profits per unit resulting from the uplift in land values rose by **36% to £68,300, equivalent to 29% of the value of the average house** in England in 2017.

In order to unlock this huge funding potential and dramatically increase investment in affordable housing and infrastructure, three key steps are necessary.

First, every functional economic area needs to develop integrated transport and housing plans. These plans should aim to increase housing supply while ensuring that households have access to improved public amenities and are connected to places of work.

Second, the relevant public authority needs to lead the land assembly process in partnership with developers and other key stakeholders to put in the necessary infrastructure before releasing serviced plots to housebuilders and individuals for self-builds.

275x

Land awarded planning permission is worth more than 275 times agricultural value

Third, to fund the much-needed infrastructure, the public authority will need to capture as much of the £10.7bn of windfall profits per annum given current section 106 and CIL contributions are insufficient to help fund large scale projects. This can be achieved through further reform of the land market by removing prospective planning from the compensation arrangements. Such a reform builds on the existing no-scheme world principle set out in the 1961 Land Compensation Act.

By redirecting the annual gains of £10.7bn from the granting of planning permission to help fund more infrastructure, housing output can rise further providing huge opportunities for SME builders and housing associations. Prior analysis indicates this could increase the rate of new builds to somewhere close to 280,000 units per year with sufficient funding for around 100,000 affordable housing units.[1] This would bring total output for England including conversions to the government's target of 300,000 units a year.

1 Centre for Progressive Policy (2018) Press Release: *How reforming the land market can help deliver the government target of 300,000 new homes per year*. Available at: https://progressive-policy.net/2018/04/press-release-how-reforming-the-land-market-can-help-deliver-the-government-target-of-300000-new-homes-per-year/

Introduction

Over the last few years there has been a growing cross-party consensus that to raise the rate of housebuilding, three key issues need to be addressed.

The first is the requirement to **integrate infrastructure and housing plans across functional economic areas** which generally equate to city or county regions.[2] The second is that there needs to be a **public-led land assembly** process that delivers the infrastructure providing serviced plots for housebuilders and individuals for self builds. Third, is that the **community should be able to benefit more from the rise in land values** to improve the viability of infrastructure and housing projects.

> During the 2017 General election campaign both Labour and Conservative parties outlined the desire to look at how a greater proportion of land values might be captured, as did the government's Housing White Paper published in 2017.

Previous empirical research by the Centre[3] on land value capture which has been widely cited estimated the proportion of land value increases that are currently being captured and how much is flowing through to landowners, promoters and developers as the result of planning permission awards. The Centre in conjunction with its team of legal advisors has also advocated amending the 1961 Land Compensation Act to remove prospective planning permission from the compensation arrangements as well as Certificates of Appropriate Alternative Development. This would enable these windfall profits to flow instead to local authorities to help fund new infrastructure and affordable housing.[4]

In November 2017, the former Conservative planning minister Nick Boles MP argued for a similar policy citing the way things work in Germany where 'local councils take the lead in acquiring land for major developments and putting in the necessary basic infrastructure – roads, sewers and utilities as well as parks and schools – before selling off serviced plots so that private developers can start building houses.'[5]

In February 2018, the shadow housing minister John Healey argued that a Labour government would enable the public acquisition of land at nearer pre-planning permission value through reform of the 1961 Land Compensation Act,[6] and in June 2018, Vince Cable, the leader of the Liberal Democrats announced a similar policy.[7]

More recently, Onward, a new Conservative think tank, has argued that a greater portion of the uplift in land values resulting from planning permission awards should be captured by local authorities to fund the necessary infrastructure to improve support for development and housebuilding.[8]

In addition to this cross-party support in Westminster, the MHCLG Select Committee has set up an inquiry into land value capture[9] and there is also an All Party Parliamentary Group on land value capture.[10]

Land compensation is a devolved matter and in Scotland there is increasing interest in reforming the land compensation arrangements. An amendment to the recent Scottish Planning Bill has been submitted by Andy Wightman MSP of the Scottish Green Party to change the compensation rules,[11] and a speech by Ruth Davidson MSP, leader of the Scottish Conservatives, suggests that there is growing support for change across the political spectrum in Scotland.[12]

---

2 National Infrastructure Commission (2016), *Review of the Case for Large Scale Transport Investment in London.* Available at: https://www.nic.org.uk/wp-content/uploads/Review-of-the-Case-for-Large-Scale-Transport-Investment-in-London.pdf
3 The Centre for Progressive Capitalism merged with the newly founded Centre for Progressive Policy in March 2018
4 Aubrey, T. (2016) *Bridging the Infrastructure Gap: Funding the Infrastructure and Affordable Housing for the East West Corridor.* Centre for Progressive Policy. Available at: https://progressive-policy.net/wp-content/uploads/2016/06/Bridging-the-infrastructure-gap-June-2016.pdf
5 Square Deal (2017) *Square Deal on Housing*. Available at: http://www.squaredeal.org.uk/square-deal-for-housing/
6 Booth, R. (2018) *Labour plans to make landowners sell to state for fraction of value*. The Guardian. Available at: https://www.theguardian.com/politics/2018/feb/01/labour-plans-landowners-sell-state-fraction-value
7 Walker, P. (2018) *Lib Dems propose land-buying agency to boost house building*. The Guardian. Available at: https://www.theguardian.com/society/2018/jun/26/lib-dems-vince-cable-land-buying-agency-to-boost-house-building
8 Onwards (2018) *Green, pleasant and affordable: Why we need a new approach to supply and demand to solve Britain's housing problem*. Available at: http://www.ukonward.com/wp-content/uploads/2018/06/220618-Green-Pleasant.-Affordable-Web-ready.pdf
9 Communities and Local Government Committee (2018) *Land value capture inquiry.* Available at: https://www.parliament.uk/business/committees/committees-a-z/commons-select/communities-and-local-government-committee/inquiries/parliament-2017/land-value-capture-inquiry-17-19/
10 All Party Parliamentary Group (2018) *Land Value Capture*. Coalition for Economic Justice. Available at: http://www.c4ej.com/appg. See also House of Commons, Housing, Communities and Local Governme 'Land Value Capture, Tenth Report of Session 2017–19', Available at: https://publications.parliament.uk/pa/cm201719/cmselect/cmcomloc/766/766.pdf
11 Local Government and Communities Committee (2018) *Planning (Scotland) Bill*. Getting Involved: Scottish Parliament. Available at: http://www.parliament.scot/parliamentarybusiness/Bills/106768.aspx
12 Davidson, R. (2018) *Ruth Davidson - Building a stronger future for Britain*. Policy Scotland. Available at: https://policyscotland.gla.ac.uk/ruth-

The Scottish government has tasked the Scottish Land Commission to provide direction and leadership on the ownership, management and use of land and buildings that contributes to the collective benefit of everybody. The Commission is expected to publish a report in the Autumn on the issue.

Although there is an emerging political consensus that a greater share of the uplift in land values needs to be captured by public authorities, a number of stakeholders have also emerged to oppose potential change to the compensation arrangements.[13]

Set against this backdrop, the purpose of this report is twofold.

First, is to update our initial land value capture analysis using updated land values for 2017.[14] The publication of a more detailed set of data in addition to comments we have received on improving our methodology means we are now able to provide updated estimates on the uplift in land values.

Secondly, the report aims to provide a more detailed explanation as to why our proposed reforms to the 1961 Land Compensation Act would lead to broader changes in the land market, and hence would not require land to be purchased through a Compulsory Purchase Order (CPO) mechanism. Such a change would require large-scale developments to be driven by a public-led land assembly process in partnership with private sector stakeholders.

Section 1: Empirical analysis

In 2016, the then Centre for Progressive Capitalism developed a methodology to estimate the uplift in land values from initial use value to residential value for England for 2014/15 based on published MHCLG data. The objective of the analysis was to better understand how well England was already capturing land values which might explain why the level of infrastructure investment in the UK is so low when compared internationally, and also why the rate of housebuilding has been so much lower than in other economies.

The consultancy McKinsey & Co estimated the UK infrastructure stock as a percentage of GDP at only 57% compared to Germany with 71%. Furthermore, UK housebuilding rates per capita trail other countries by a considerable amount, with the Netherlands building nearly 70% more units per capita than the UK since the mid-1970s.[15]

The initial empirical analysis suggested that around a quarter of the uplift was being captured, and that windfall profits or the unearned income arising from the award of planning permission was over £9bn for that fiscal year.[16] Clearly the amounts will change from year to year depending on land prices, housing output and density levels.

The publication of a new set of land values for 2017 enables the analysis to be updated and improved in light of other recently published research. Such an analysis will enable policy makers to understand to what extent windfall profits have increased and whether government policy has made much of a difference. It will also provide indications to local and national policy makers how much incremental funding for infrastructure projects and affordable housing could become available should the land market be reformed.

i) Estimating existing use value of undeveloped land for new builds

The initial use value of the land based on the 2016/17 data is estimated at £3.122bn.

The analytical approach undertaken in this report for the new Centre for Progressive Policy is broadly similar to the prior 2016 report which utilises updated land prices, density data and new build completions by local authority published by MHCLG.[17] Some improvements were made to the methodology based on comments we have received. To improve accuracy, the land use analysis was undertaken at the more detailed local authority level rather than London versus the rest of England. This enabled the study to exclude all units built on previously developed residential land which accounted for 18% of the units, as the land sitting under those units had already been awarded planning permission.

For previously developed land excluding residential land, LEP-based industrial values per hectare were used. Land with existing buildings converted to residential use (which would have higher land values) were not included in the analysis as converting existing buildings to residential dwellings is counted for separately in the housing statistics.

davidson-lecture-full-text/

13 Compulsory Purchase Association (2018) *Written evidence submitted by the Compulsory Purchase Association*. Available at: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/housing-communities-and-local-government-committee/land-value-capture/written/79378.html

14 Ministry of Housing (2018) *Land value estimates for policy appraisal 2017*. Available at: https://www.gov.uk/government/publications/land-value-estimates-for-policy-appraisal-2017

15 Aubrey, T. (2016) op cit.

16 Aubrey, T. (2018) *Estimating land value capture for England – updated analysis*. Centre for Progressive Policy. Available at: https://progressive-policy.net/2017/03/estimating-land-value-capture-england-updated-analysis/

17 See appendix A for full methodology.

Indeed, the net change of use now accounts for more than 37,000 additional dwellings per year, with around half of these built under permitted development rights.

Agricultural land values at the LEP level were used for non-previously developed sites although the use value was increased for the 6% of units that were built on residential gardens.[18]

The increase of £2.383bn from the 2014/15 data can mostly be explained by the fact that more units have been built and industrial land values have risen. The improved methodology has also increased the use value estimate.

ii) Estimating residential value of land for new builds

The residential value of the land based on 2016/17 data is estimated at £21.481bn.

The housing output data and residential land values by local authority, in conjunction with the average density figures by local authority enables the total residential value of land built on over the 2016/17 period to be estimated. The density data is measured using the ONS mapping approach which takes account of all existing green spaces as well as roads and other amenities needed for new units. Hence the density data by definition is a net figure in relation to a hectare of land which MHCLG provides prices for. This generates an estimate of £22.183bn.

The residential land values however do not take account of abnormal costs such as demolition and land remediation that may be incurred during development, in particular for brownfield sites. Clearly, larger brownfield sites are likely to have higher abnormal costs whereas greenfield sites few abnormal costs. It is difficult to estimate what an average abnormal cost estimate for England might be given that local authorities do not publish data on abnormal costs.

For this analysis, an average abnormal cost of £130,000 per hectare is assumed, which can be scaled up across the estimated 5,400 hectares that were built on during the 2016/17 period. This would in effect reduce residential land values by the amount of abnormal costs of around £0.7bn.[19] Hence the residential value is estimated to be £21.481bn.

The dramatic increase in the value of residential land for new builds can be explained by the fact that the industry has accelerated housing output since 2014/15 – up by 18%. In addition, there has been a significant jump in average residential land values of nearly 38%. Average house prices grew by around 16% during the period.[20]

38%
Average increase in residential land value 2014/15-2016/17

16%
Average increase in house prices 2014/15-2016/17

In an upswing it is typical for land prices to grow faster than house prices. However, as house prices begin to fall, which is currently happening in London[21], land prices tend to fall much faster, hence the very nature of these calculations can vary over time.

iii) Estimating captured land values

The amount being directly captured by local or central government is estimated at £5bn.

One of the most important ways of capturing the increase in land values is from section 106 contributions and the community infrastructure levy (CIL). The latest data based on a survey carried out for MHCLG is that for 2016/17 the total value of committed contributions was £6.007bn, the bulk of which is for affordable housing and CIL.[22] The study stated that nearly 100% of 106 contributions were related to residential development, however, it is feasible that some commercial development contributions are being captured via CIL.

Although £6bn has been committed, actual payments are contingent on sites that actually get built out. As noted in a recent report, between 30-40% of planning permissions lapse and between 10-20% of planning permissions never materialise into a start while a further 15-20% are recycled into a further application.[23] Furthermore, as highlighted by MHCLG, 65% of planning authorities renegotiated a planning agreement in 2016/17.[24] Hence it is clear that although £6bn has been committed, £6bn will not be captured.

In estimating what might have been captured based on MHCLG figures, we assume that 30% of the planning permissions lapse, half of which are recycled into future contributions. In addition, the widespread renegotiation of planning agreements reduces amounts paid. Hence

18 See appendix A for estimate on residential gardens.
19 £130,000 data point sourced from Gleeds (2012) *Abnormal Site Development Costs*. Available at: https://www.newark-sherwooddc.gov.uk/media/newarkandsherwood/imagesandfiles/planningpolicy/pdfs/allocationsdevelopmentmanagmentoptionsreport/allocationsanddmdpo-examination/EB41%20Gleeds%20Abnormal%20Site%20Development%20Costs%20Appraisal.pdf
20 HM Land Registry (2018) *Compulsory Purchase: Written question – 125518*. UK Parliament. Available at: https://www.gov.uk/government/statistical-data-sets/uk-house-price-index-data-downloads-june-2018
21 Nationwide (2018) *House Price Index - Annual house price growth slows to a five-year low in June*. Available at: https://www.nationwide.co.uk/-/media/MainSite/documents/about/house-price-index/2018/Jun_Q2_2018.pdf
22 Ministry of Housing (2018) *Section 106 planning obligations and the Community Infrastructure Levy in England, 2016 to 2017: report of study.* Available at: https://www.gov.uk/government/publications/section-106-planning-obligations-and-the-community-infrastructure-levy-in-england-2016-to-2017-report-of-study
23 Walker, C. (2017) *The role of land pipelines in the UK housebuilding process*. Available at: https://cweconomics.co.uk/wp-content/uploads/2017/10/CWEconomicsReport_Land_Banking.pdf
24 Ministry of Housing, Communities & Local Government (2018) *Supporting housing delivery through development contributions.* Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/691182/Developer_Contributions_Consultation.pdf

it is assumed that around one third of the amount committed would not be contributed, hence a figure of £4bn is a reasonable estimate of what has actually been paid.

Besides being able to extract this £4bn from rising land values, the state is also able to generate income from the sale of public land. According to MHCLG, the public land for housing programme sold plots for 8,444 units between 2016/17 although no monetary value has been disclosed.[25] The government plan was to sell £1bn of land per year,[26] but it failed to meet this target as noted in a highly critical NAO report.[27] CPP analysis here assumes that the government has been able to learn from this criticism and increase land sales to meet its initial target of £1bn.[28]

Although the absolute amount captured of £5bn has increased since 2014/15, so have house prices and land values. The amount directly captured as a percentage of the total uplift has remained roughly the same at 27% of the uplift compared to 25% in 2014/15. This indicates that windfall profits have increased in absolute terms due to rising land values.

v) Estimating windfall profits

Pre-tax windfall profits for 2016/17 estimated at £13.359bn.

The total increase in land values can be estimated by taking the use value from the total residential value (£21.481bn - £3.122bn) which equates to £18.359bn. Removing the £5bn that has already been captured leaves £13.359bn as the estimated windfall profit.

While the largest amount of land uplift accrues to areas such as London with the highest land values, it is important to note that many regions of England stand to benefit substantially from any reform that increases the amount of land value captured.

The map on the following page is set up by functional economic area based on LEPs to indicate the total uplift estimated based on 2017 land prices, housing output and density. For consistency reasons we have excluded the payments from section 106/CIL and land sales, as we do not have sufficient data at the local authority level to compute this with any degree of accuracy.

Outside of London and the South East, the following regions indicate a substantial increase in land values which when forecast over a 20-year period could provide a substantial revenue stream to support new infrastructure investment and affordable housing.

Table 1: Top 10 land value uplift by LEP outside of the South East

LEP	Annualised uplift £m	20 year uplift £m
South East Midlands	858	17,160
Birmingham City Region	563	11,260
Heart of the South West	490	9,800
New Anglia	399	7,980
Cheshire and Warrington	315	6,300
West of England	288	5,760
Leicester and Leicestershire	278	5,560
Gloucestershire	276	5,520
North East	247	4,940
Leeds City Region	237	4,740

Source: MHCLG, Centre for Progressive Policy

Note: Birmingham City Region is an aggregation of the Birmingham & Sollihull, Coventry & Warwickshire and Black Country LEPs.

> While the overall amounts of uplift have increased for England over the last 2 years, the picture across the country is quite varied.

London shows a significant increase from 2014/15 in addition to a number of other core city regions. However, not all regions have demonstrated an increase in uplift over the period with Manchester, Sheffield and Liverpool showing falls in the amount of land value uplift.

Infrastructure costs tend to be lower outside of London and the South East, hence despite lower land values, the increase in value from use to residential value remains of interest in terms of helping fund infrastructure and affordable housing in all city regions.

25 Homes and Communities Agency (2017) *Annual Report and Financial Statements 2016/17*. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/627166/HCA_AR16-17.pdf
26 National Audit Office (2015) *Disposal of public land for new homes*. Available at: https://www.nao.org.uk/report/disposal-of-public-land-for-new-homes/
27 National Audit Office (2016) *Disposal of public land for new homes: a progress report.* Available at: https://www.nao.org.uk/report/disposal-of-public-land-for-new-homes-a-progress-report/
28 Should further information come to light then this figure would need to be adjusted as the estimate may well be too high.

Chart 1: Total uplift excluding land value already captured

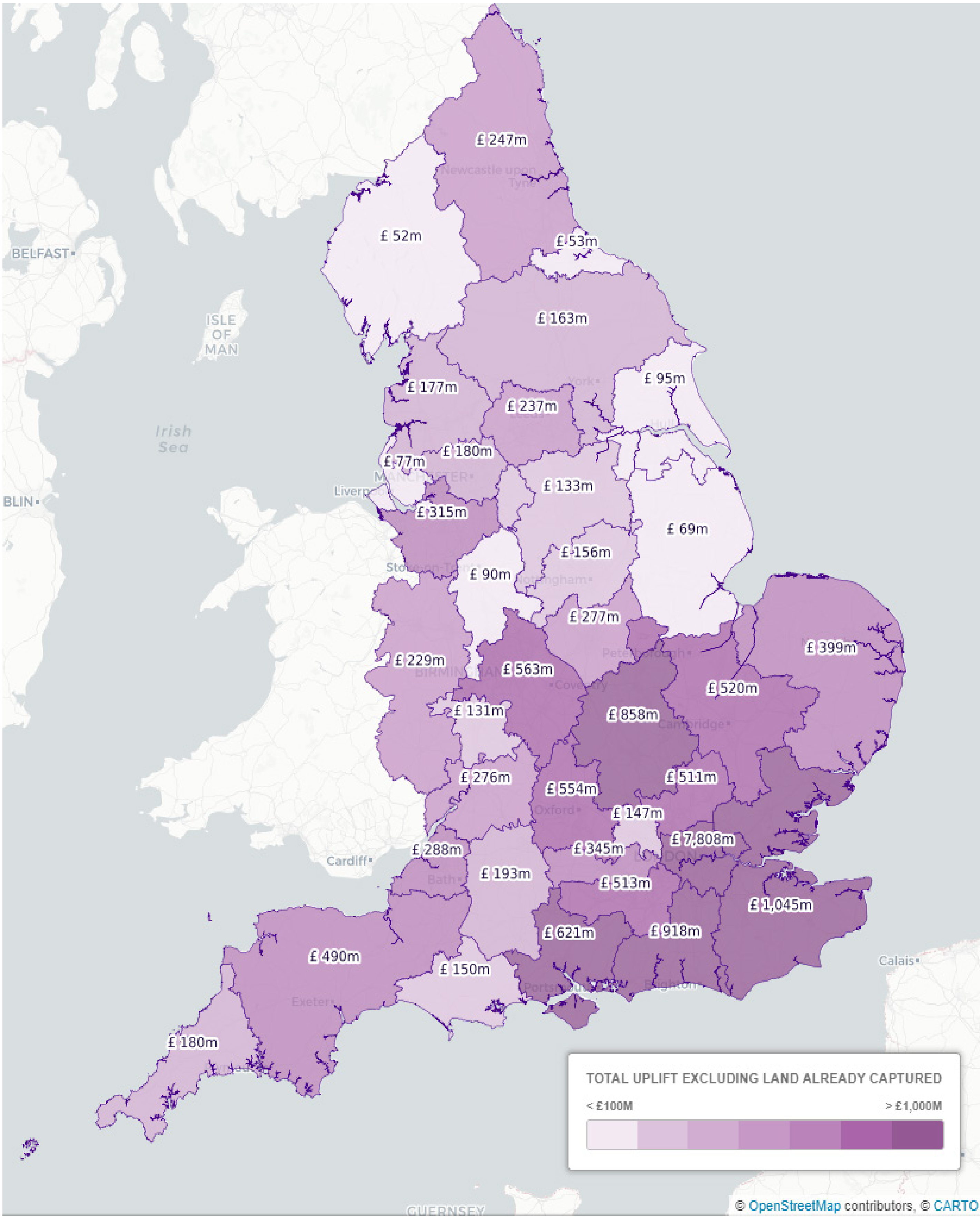


Table 2: Change in land value uplift across Core City regions and London 2014/15 to 2016/17

LEP	2014/15 uplift in land values £m	2016/17 uplift in land values	% change
London	4,752	7,808	64%
Birmingham City Region	444	563	27%
West of England	213	288	35%
North East	223	247	11%
Leeds City Region	190	237	25%
Greater Manchester	183	180	-2%
D2N2	143	156	9%
Sheffield City Region	169	133	-21%
Liverpool City Region	81	77	-5%

Source: MHCLG, Centre for Progressive Policy

From a public policy perspective, the above table suggests that London could become self-sufficient in funding infrastructure and affordable housing should it be able to access this uplift in land values, which would free up the budget allocated to London for other areas in need.

Windfall profits adjusted for tax are estimated at £10.689bn for 2016/17 or £214bn over 20 years.

The tax system has been set up to capture some of this uplift including a tax on the acquisition of land through stamp duty land tax. An individual would need to pay capital gains tax above a specified amount at a particular rate, and corporations will also pay corporation tax on profits. If an individual is deemed to be trading in land, then they might be liable for income tax instead of capital gains tax.

- Stamp duty land tax: A 5% tax is levied on transactions above £250,000, with stepped rates below this (0% on first £150,000 and 2% between £100,000 and £250,000) on the acquisition of land above a certain amount. However, if a company is acquired that owns the land instead, then stamp duty costs are only 0.5% which is the rate for share transactions.

- If the entity that generates windfall profits is an individual, then he/she is liable to pay capital gains tax at 20% as long as the land has not had dwellings built on it. If the individual is considered to be "trading" then they might be liable for income tax instead of up to 45%. If the entity is a company, then 20% corporation tax is liable. However, this does not necessarily mean that this is the level of tax that gets paid. For example, debt interest costs can be written off against tax liabilities reducing corporation tax.

  In addition, the landowner might be able to claim entrepreneurs tax relief of 10%.[29]

Due to the ability of economic agents to minimise their tax liabilities through perfectly legitimate means, it is unclear how much central government might be capturing indirectly. Until more of this kind of tax data is made available, it is very difficult to ascertain exactly how much tax is being paid as a result of land transactions.

Given the various approaches to minimising tax liabilities, it is highly doubtful that the government is capturing anything close to the full 25% of the windfall profits (assuming 5% stamp duty land tax, CGT at 20% or corporation tax at 20%). A tax rate of 20% therefore might be a reasonable estimate.

Hence if the windfall profits of £13.359bn are adjusted to take account of a 20% tax take, post-tax windfall profits would be £10.689bn, suggesting that 58% of the uplift flows through to windfall profits. Top-down estimates submitted to the housing communities and local government land value capture committee implied that after tax, landowners are capturing around 51% of the uplift.[30]

£10.689bn of windfall profits amounts to £68,299 per unit based on housing output of 156,474.[31] Average house prices for England in May 2017 were £236,727, hence windfall profits are equivalent to 29% of the value of an average house brought to market in England in 2017.

One further point to consider is that England remains highly centralised in terms of fiscal policy. Although local authorities have awarded planning permission, a reasonable portion of the captured uplift flows directly to central government via taxation instead.

> If local authorities are going to have to invest in future infrastructure to accelerate housebuilding, it would be more beneficial if a greater share of the uplift flowed directly to them.

Who profits from the uplift?

There are broadly three segments of the market that have been able to benefit from the uplift in values resulting from the awarding of planning permission including: landowners, promoters & intermediaries, and to a lesser extent, volume housebuilders.

The challenge of estimating the exact portion captured by each segment is not possible due to the paucity of data, although landowners are the main beneficiaries as a result of the monopoly effect of owning land in high demand areas.

---

29 Dixon, S. (2018) *Selling UK land: useful tax points for landowners.* RICS. Available at: https://www.isurv.com/info/390/features/11508/selling_uk_land_useful_tax_points_for_landowners

30 Crook, T. (2018) *Written evidence - Professor Tony Crook*. Available at: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/housing-communities-and-local-government-committee/land-value-capture/written/79512.html

31 This figure is lower than the figure in table 120 due to the removal of all units built on previously developed land.

It has been estimated that land promoters might earn between 10% to 30% of the increase in land value should a sale go through,[32] and other intermediaries might be expected to earn in the low single digits due to the nature of the transactional services provided.

With regards to volume housebuilders, an analysis of the trends in gross margins shows the industry over the last four years has reached record levels as land values have risen.

The volume housebuilders' gross income according to the Datastream UK housebuilders index is £6.794bn for 2017.[33] Furthermore, by the industry and government's own admission there has been almost no productivity increase within the construction sector since 1994.[34] This suggests that rising productivity is unlikely to have been the main driver of the recent increase in gross margins, hence the increase is likely to have come from other sources of profits, of which rising land values is clearly one possibility.

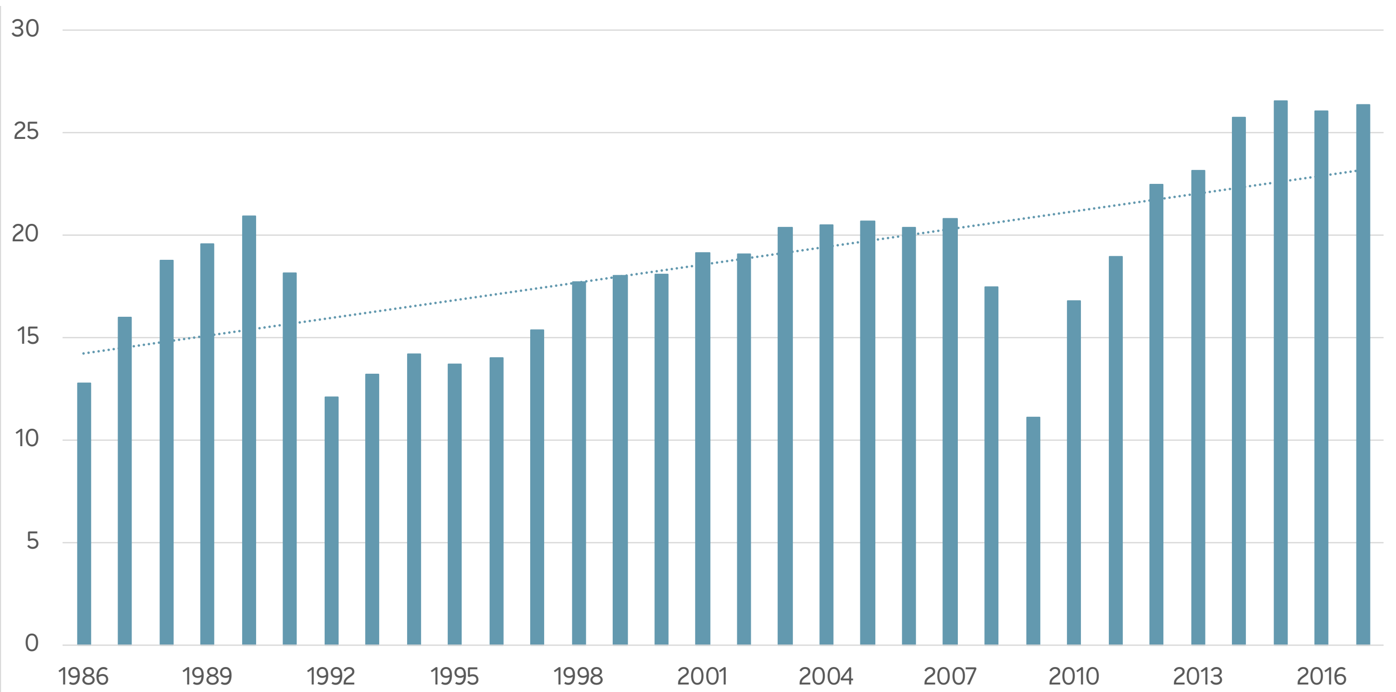
One property analyst, for example, has illustrated the importance of land to the rising profits of Taylor Wimpey and Persimmon. Furthermore, the Berkeley Group warned in June 2018 that its profits are set to fall as it runs out of cheap land acquired in the aftermath of the financial crisis.[35]

The question for public policy is to what extent do these large windfalls to landowners, promoters, and to a lesser extent, volume housebuilders merely reflect the business model of building houses in England? And to what extent is this approach typical across other European countries?

Land market structure: speculative vs public-led assembly.

In countries with higher rates of housebuilding and infrastructure investment such as France, Germany and the Netherlands, local government plays a key role in developing an integrated transport and housing plan.[36] Once the plan is agreed, the land is generally assembled through a development corporation which often includes firms developers that put in the infrastructure, thereby delivering serviced plots to housebuilders and individuals to build on.

One critical difference between these countries and England is that this approach captures a far greater proportion of the increase in land values arising from the awarding of planning permission. The availability of this source of funding increases the viability of implementing large scale projects, including the provision of infrastructure and affordable housing. This is similar to how the garden cities and new towns were developed in the UK in the early and mid-part of the 20th century.



32 Fraser, I. (2017) *The modern-day barons: inside the murky underbelly of land promotion*. The Telegraph. Available at: https://www.telegraph.co.uk/business/2017/08/05/modern-day-barons-inside-murky-underbelly-land-promotion/

33 The index contains 12 constituents.

34 Farmer, M. (2016) *The Farmer Review of the UK Construction Labour Model. Construction Leadership Council*. Available at: www.constructionleadershipcouncil.co.uk/wp-content/uploads/2016/10/Farmer-Review.pdf

35 Hudson, N. (2018) 21 August. Available at: https://twitter.com/resi_analyst/status/1031861232184320001; Hudson, N. (2018) 28 February. Available at: https://twitter.com/resi_analyst/status/968809794944618496; Hudson, N. (2018) 27 February. Available at: https://twitter.com/resi_analyst/status/968423151532208129; Knowles, T. (2018) Berkeley warns of profits slump as stock of cheap land runs out. The Times. Available at: https://www.thetimes.co.uk/article/bb7858cc-745c-11e8-a95e-4d8f3c5d626c

36 Hall, P. with contributions from Nicholas Falk (2013) *Good Cities, Better Lives: How Europe Discovered the Lost Art of Urbanism*. Routledge; Falk, N. (2018) Capital Gains, a better land assembly model for London. Available at: https://www.london.gov.uk/sites/default/files/gla_capital_gains_report_.pdf

But this approach in England is today atypical. Development is largely speculative in nature and carries a lot of risk for housebuilders. Given that the supply of residential land in high demand areas is limited by location, speculative developers are forced to bid for land prices upfront. Once a site is acquired and has been granted planning permission, developers will aim to build out units to meet demand at certain price thresholds in order to meet their profit hurdles and fulfil their obligations to their shareholders.

> The challenge for housebuilders is that unless there is adequate infrastructure in place, then there will be less demand for housing. People need to be connected to jobs and close to schools and hospitals.

The question remains, therefore, who will provide the necessary infrastructure to further raise the rate of housebuilding? The Peace Review of CIL in 2017 indicated that the community infrastructure levy is unlikely to provide the necessary scale of funding for the infrastructure that the country so desperately needs.[37]

Instead, the Centre for Progressive Policy argues that a more viable solution is to reform the land market so that a greater share of the uplift in land values can be used to fund new garden cities, towns and urban extensions.

Section 2: Reform of the land market

The emerging cross-party consensus to capture a larger amount of the uplift in land values to help fund infrastructure investment and affordable housing has led to debate on how best this might be achieved.

> The Centre recommends reform of the land compensation arrangements in conjunction with driving development at scale through a public-driven, land assembly process.

More specifically it is recommended that the 1961 Land Compensation Act is amended so that:

- No account is taken of any prospective planning permission in land designated by local authorities for infrastructure including housing.
- Certificates of appropriate alternative development would cease to apply in those areas designated by local authorities for development.[38]

The ability to capture the uplift from selling serviced plots would improve the viability of large scale developments given that it would provide significantly larger funding streams to pay for both infrastructure and affordable housing. This would bring England more in line with France, Germany and the Netherlands.

Our analysis of the proposed infrastructure investment along the Oxford-Milton Keynes-Cambridge corridor (East West corridor) suggests that the uplift in land values, in combination with other funding streams, would not only be sufficient to fund the infrastructure but also provide a subsidy for around 36% of units to be affordable housing.[39]

In the event that private or public landowners did not want to become a risk sharing partner of the scheme, the amended land compensation arrangements would result in land transacting at market values closer to use value for the development. This policy would not require every public-led land assembly project to be driven by a compulsory purchase order (CPO) in the event that public and private landowners were unable to agree on pooling their land for the development. The compensation arrangements in conjunction with the threat of a CPO would be sufficient to improve the efficient functioning of the land market. This is how land markets operate in France, Germany and the Netherlands, where CPOs are not particularly common.

France, Germany & The Netherlands

All markets are a function of the rules that have been set up to create that market. In land markets, the compensation arrangements, where the state acquires land on a compulsory basis, impact the broader land market given that a buyer might have to sell its land to a public body at any point in time. The development of law in this area has therefore a significant impact on the nature of land market transactions. For example:

> in France, the Netherlands and Germany, the ownership of land does not include a right to the development value that results from urban growth in general.[40]

---

37 Community Infrastructure Levy (2016) *A New Approach to Developer Contributions*. Available at: https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/589637/CIL_REPORT_2016.pdf
38 These specific legal recommendations were made by our team of QCs who continue to provide support to the CPP.
39 Aubrey, T. (2017) *Funding the Infrastructure and Affordable Housing for the East West Corridor*. Centre for Progressive Capitalism. Available at: https://progressive-policy.net/wp-content/uploads/2017/10/Financing_East_West_Online.pdf
40 See Renard, V. (2009) *Property Rights Protection and Spatial Planning in European Countries*. In G. K. Ingram and Y. Hong (eds.) Property Rights and

In the Netherlands, the Land Readjustment Act has enabled Dutch municipalities to assemble land which up until the 1990s was acquired at roughly twice agricultural value in the event where the owner did not want to participate in the scheme. The compensation arrangements require the municipality to compensate at the average land value for the development of the project. As offers were given at these values, there was no need to pursue a CPO.[41] The legislative framework therefore provides the market with the necessary signals to function in an efficient manner.

The situation has changed slightly in the Netherlands as a result of rising house prices which has made it more profitable for developers to undertake development, which in turn has put pressure on the prices at which local authorities are able to acquire agricultural land for development. More recent data suggests that public authorities are acquiring land at close to ten times agricultural values rather than twice.[42] Despite this increase in the level at which land is acquired from owners not wishing to participate in the scheme, around 90% of the uplift in land values is captured to help fund infrastructure and affordable housing.

> The Netherlands has built nearly 70% more units per capita than the UK since the mid-1970s. Funding infrastructure by utilising the increase in land values has proven to be central to this success story.

In France, smaller scale projects are generally developed through a *zone d'aménagement concerté* or a ZAC where public and private landowners pool their land. For larger scale projects, this can be undertaken through a *société publique locale* or SPL, which replaced the *sociétés d'economie mixte locales* or SEML [43]. The Urban Code in France is based on the principle of non-compensation where local authorities have pre-emption rights on private land.[44]

In Germany, as highlighted by Nick Boles in his *Square Deal for Housing*, Freiburg was able to acquire the land close to use value and use the uplift to help fund infrastructure and affordable housing. The German Federal Building Code or *Baugesetzbuch* enables municipalities through urban development zones to acquire undeveloped or derelict land with reference to market values as set out in section 169. Market values as described in section 194, are values at which transactions are made that take "into account the existing legal circumstances and the actual characteristics" of the land. This enables German municipalities to capture most of the increase in land value which is used to fund the infrastructure that unlocks new land for housing.

90%

Estimated uplift of land value captured in the Netherlands.

The similarities between France, Germany and the Netherlands were also highlighted by a study commissioned by the Dutch government to assess the compensation arrangements between the three countries. According to the report, all three countries "share an outlook in that property is socially bound and the damage caused by government acts is a component of the social risk that individuals run as residents of those countries." The study also found that the Dutch compensation arrangements had become overly generous, which subsequently resulted in a tightening of the compensation rules.[45] This suggests that greater than 90% of the uplift in land values is being captured in France and Germany.

Interventions and market prices in the UK

In the UK, past government interventions in the land market, including the compensation arrangements, have played a significant role in the price at which land is acquired for development.[46] The first major intervention by the British government related to compensation levels impacting land prices was the *1845 Land Clauses Consolidation Act*. The Act required that 'regard to be had to the value of the land to the owner' which led to buyers of land acquiring land at roughly a 10% premium to "market values".[47]

As the First Word War drew to a close, the government expected that public authorities would need to acquire large

Land Policies – proceedings of the 2008 Land Policy Conference.

41 See Needham, B. (2007) The Search for Greater Efficiency: Land Readjustment in the Netherlands. In Y. Hong and B. Needham (eds.) *Analysing Land Readjustment*. Available at: https://www.lincolninst.edu/sites/default/files/pubfiles/analyzing-land-readjustment-full.pdf

42 Segeren, A. (2007) *de grondmarkt voor woningbouwlocaties belangen en strategieën van grondeigenaren. Planbureau voor de Leefomgeving*. Available at: http://www.pbl.nl/sites/default/files/cms/publicaties/De_grondmarkt_voor_woningbouwlocaties.pdf

43 Royal Town Planning Institute (2015) Planning as 'market maker': How planning is used to stimulate development in Germany, France and The Netherlands. Available at: https://www.rtpi.org.uk/knowledge/research/projects/small-project-impact-research-spire-scheme/planning-as-market-maker/

44 Article L 160-5 of the French Code de l'Urbanisme states that "regulations and norms that result from this code, including the prohibition to build anything, do not open a right to compensation".

45 Hobma, F. and Wijting, W. (2007) *Land-Use Planning and the Right to Compensation in the Netherlands*. Washington University Global Studies Law Review. Available at: https://openscholarship.wustl.edu/cgi/viewcontent.cgi?article=1127&context=law_globalstudies

46 It has been argued recently that compensation arrangements do not impact market prices. See http://www.compulsorypurchaseassociation.org/land-value-capture.php

47 Barnes, M. (2014) *The Law of Compulsory Purchase and Compensation*. Hart Publishing.

quantities of land for public purposes and established the Scott Committee in 1918 which led to the Acquisition of Land (Assessment of Compensation) 1919 Act. The Scott Committee argued that:

> *"In our opinion, no landowner can, having regard to the fact that he holds his property subject to the right of the State to expropriate his interest for public purposes, be entitled to a higher price when in the public interest such expropriation takes place, than the fair market value apart from compensation for injurious affection"*
>
> (Scott Committe, 1918)

The conclusion of the Scott Committee resulted in the introduction of the "market value" principle, which was that compensation for the land taken should be based on the market value as between a willing seller and a willing buyer", with no special allowance for compulsory acquisition.[48] The impact of the legislation was that the values at which land was transacted at fell, eliminating the 10% premium that the 1845 Act had conferred on market values.

Following the Second World War, the Labour government essentially nationalised development rights stating that land was to be acquired at use value rather than market values. The system did not work as expected and in 1959 the Town and Country Planning Act repealed the 1947 Act and reinstated the 1919 Act market principle.

The 1961 Act consolidated the 1959 and 1919 Acts and crucially implemented the no-scheme world principle. The no-scheme world or point gourde principle disentitles landowners from compensation for any uplift in value arising from the scheme itself. For example, the increase in residential land values arising from a new train line put in at public expense could not in most circumstances be claimed by the landowner.[49] This piece of legislation once again impacted market values which were reduced by the amount of value added by the scheme funded by public authorities.[50] Compensation arrangements play a major role in signalling to the market how land is valued.

One point that has been raised in the debate is that the new towns such as Milton Keynes continued to be built subsequent to the 1961 Act, implying that the compensation arrangements per se are not preventing development at scale. The evidence from Milton Keynes shows that the new towns actually continued to acquire land at values close to agricultural values based on the principle that there was no value outside of the scheme. This was subsequently challenged by Myers in the case against Milton Keynes Development Corporation.[51]

The result of this case is that instead of acquiring land at market prices of just over twice agricultural values, future towns would need to acquire land (assuming similar characteristics to Milton Keynes) at values closer to 20% of residential value. As residential and agricultural values have diverged dramatically, this increase has significantly reduced the viability of these kind of projects.[52]

More recently land prices have been impacted by section 106[53] and CIL[54] levies, with these interventions reducing market values to a certain extent. Therefore, the idea that land prices do not adjust to legislative changes including the compensation arrangements is not born out by the evidence. As a result of the cited legislative changes, land values have clearly adjusted to new levels.

In our view, removing prospective planning permission from the compensation arrangements is merely building on the body of law since 1919 that has used legislation to send signals to the land market. In addition to disregarding the "scheme" or the increase in value resulting from public investment, the proposed legislative framework would disregard hope value, which itself is a product of a prospective decision by the community to award planning permission. In this new environment, land speculators would be taking huge risks by buying land including hope value, given that the land might appear in a large-scale development plan and thus would be subject to these new rules.

The approach in France, Germany and the Netherlands suggests that once these signals are clear to all market participants, then the market will begin to function more efficiently. Landowners will realise there is no point holding out against a development plan, as it would merely force the public authority to CPO the land. Furthermore, landowners are likely to earn more money by accepting the offer without going to court as these offers are likely to be higher given they would provide a premium based on not having to go to court. This is why the post-war new towns such as Milton Keynes bought land at just over twice agricultural values and not at use value.

As argued these proposed reforms would reduce market values much closer to use value, which has been the case for other interventions in the land market.

48 The Law Commission (LAW COM No 286, 2004) *Towards a Compulsory Purchase Code*. Available at: https://www.lawcom.gov.uk/project/towards-a-compulsory-purchase-code/
49 The recent Neighbourhood Planning Act has introduced further amendments to the 1961 Act stating that "Where land is acquired for regeneration or redevelopment which is facilitated or made possible by a relevant transport project, the scheme includes the relevant transport project" Section 6D (3)
50 Although a form of no-scheme world was introduced in the 1919 Act, case law developed in a very narrow way until 1959 as described by Law Commission in *Towards a Compulsory Purchase Code*.
51 Myers v Milton Keynes Development Corporation Court of Appeal (1974).
52 Aubrey, T. and Bentley D. (2018) *Written evidence - Daniel Bentley and Tom Aubrey*. Available at: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/housing-communities-and-local-government-committee/land-value-capture/written/85910.html
53 Introduced in Town and Country Planning Act 1990.
54 Introduced in Planning Act 2008.

> The CPP does not propose acquiring land at less than open market value.

This distinction is an important one in law, particularly with regards to article one, protocol one of the European Convention on Human Rights (ECHR).

Some of the evidence provided to the recent select committee inquiry on land value capture argued that any changes to the current compensation code might breach the ECHR.[55] This view was countered by a senior barrister who provided evidence that there are precedents for acquiring at less than open market value where there is a significant public interest. The greater the difference between market value and the price paid—the more the government has to justify a good public interest reason why it is not paying financial equivalency.[56]

One example is the compulsory transfer of property under the *Leasehold Reform Act 1967* under which the price was calculated according to the value of the land alone, not the value of the building or the value of the merger between freehold and leasehold. Another is the *Planning Act 1990* where the Secretary of State can, in any compulsory purchase of a listed building, direct that the minimum compensation shall be paid if the owner of the building allows it to deteriorate in the hope of encouraging the prospect of demolishing and redeveloping it.

Other cases of interest include *Jahn vs Germany*[57] which led to the compulsory acquisition of agricultural land which was not in agricultural use without compensation in the context of the reunification of Germany.

In *Lithgow v UK*[58] the British government was justified in selecting a method of valuation which did not represent full market value as a result of the nationalisation of the aerospace and shipbuilding industries.

While these arguments are clearly of interest to the current debate, it needs to be emphasised that the CPP recommendation to remove prospective planning permission from the compensation arrangements is following in the tradition since 1919 of amending the rules of the land market. This would result in falling market values and therefore not require public authorities to acquire land at less than open market value.

Such a reform would result in a more efficient land market resembling France, Germany and the Netherlands where rent in its economic sense has largely been eliminated for large scale developments.

Potential implications of the policy recommendation

One implication of the proposed solution is that it requires economic regions to develop integrated transport and housing plans. The development of combined authorities and integrated transport authorities highlights that local government is already moving in this way. For example, the West of England has already published its joint spatial plan (JSP) that covers the West of England Combined Authority and North Somerset. The JSP integrates transport and housing planning across a functional economic area.[59]

> One challenge for many economic regions when it comes to infrastructure planning is that budgetary constraints tend to reduce the ambition of projects, leading to only small-scale infrastructure plans. However, the land value uplifts over an extended period of time can provide a good indication of the scale of projects that could be funded should the compensation arrangements be amended.

Research on the East West Corridor suggests that land increases could fund around half of these kind of large scale projects in addition to funds flowing from social housing receipts. Hence land values provide a good indication of the scale of ambition that JSPs should be thinking about.

The East West Corridor was supported by the National Infrastructure Commission (NIC) providing funds to develop detailed transport and housing plans. To encourage more of these plans to be developed, there is potentially a role for the NIC in conjunction with Homes England to work with functional economic areas to ensure they are at least planning at the right scale.

55 Housing, Communities and Local Government Committee (2018) *Oral evidence: Land Value Capture, HC 766*. Available at: http://data.parliament.uk/writtenevidence/committeeevidence.svc/evidencedocument/housing-communities-and-local-government-committee/land-value-capture/oral/84164.html
56 Communities and Local Government Committee (2018) *Land value capture inquiry*. Available at: https://www.parliament.uk/business/committees/committees-a-z/commons-select/communities-and-local-government-committee/inquiries/parliament-2017/land-value-capture-inquiry-17-19/
57 Jahn vs Germany (2006) 42 EHRR 49.
58 Lithgow v UK (1986) 8 EHRR 329.
59 West of England (2018) *West of England Joint Spatial Plan*. Available at: https://www.jointplanningwofe.org.uk/consult.ti

Should funding become available, then the relevant public authority would need to lead the way in assembling land with key private sector developers and landowners. These kinds of projects would generally be carried out by a development corporation that raises finance from the bond market, commissions the infrastructure and then sells off serviced plots to generate the income to pay back the bond holders. The delivery of this infrastructure may also require additional support from organisations such as Homes England and the NIC.

Such an approach would transform the way in which the city and county regions of England think about their economy and built environment. Although such a change is not straightforward, parts of England are already thinking about infrastructure and housing in this way.

Conclusion

To increase the rate of housebuilding including more affordable housing will require a significant increase in infrastructure investment opening up land for new homes. To achieve this will require functional economic areas to develop integrated transport and housing plans at scale. This raises the question of how the infrastructure might be funded.

CPP believes that the uplift in land values that successfully funded the garden cities and post-war towns, as well as large scale developments across Continental Europe, should be diverted to help fund a new wave of infrastructure investment and affordable homes.

Assuming that all taxes are being collected on the £13.4bn of windfall profits flowing to landowners, promoters and to a lesser extent, developers, this would increase investment in infrastructure and affordable housing by £10.7bn per annum or £214bn over the next 20 years. In order to take advantage of this incremental £214bn and increase the rate of infrastructure investment, the following three steps need to be followed.

First, functional economic areas at the city, county or regional level need to develop integrated transport and housing plans.

Second, it will require the relevant public authority to lead the land assembly process and put in the necessary infrastructure providing serviced plots for housebuilders and self-builds.

Third, to improve the financial viability of these projects will require the 1961 Land Compensation Act to be amended to remove prospective planning permission from the compensation arrangements. This approach, which is following in the tradition of the no-scheme world or Pointe Gourde principle and which deducts any increase in value resulting from the scheme, will lead to further falls in land prices thereby increasing the viability of projects.

Such a change could help support an increase in the rate of housebuilding of up to 280,000 units per annum of which around 100,000 would be affordable.

> An additional £10.7bn per annum or £214bn over the next 20 years to help fund new infrastructure and affordable housing that the country so desperately needs would be transformational for the economy, and for providing new homes for future generations.

Appendix A – Methodology for estimating land value capture for 2016/17

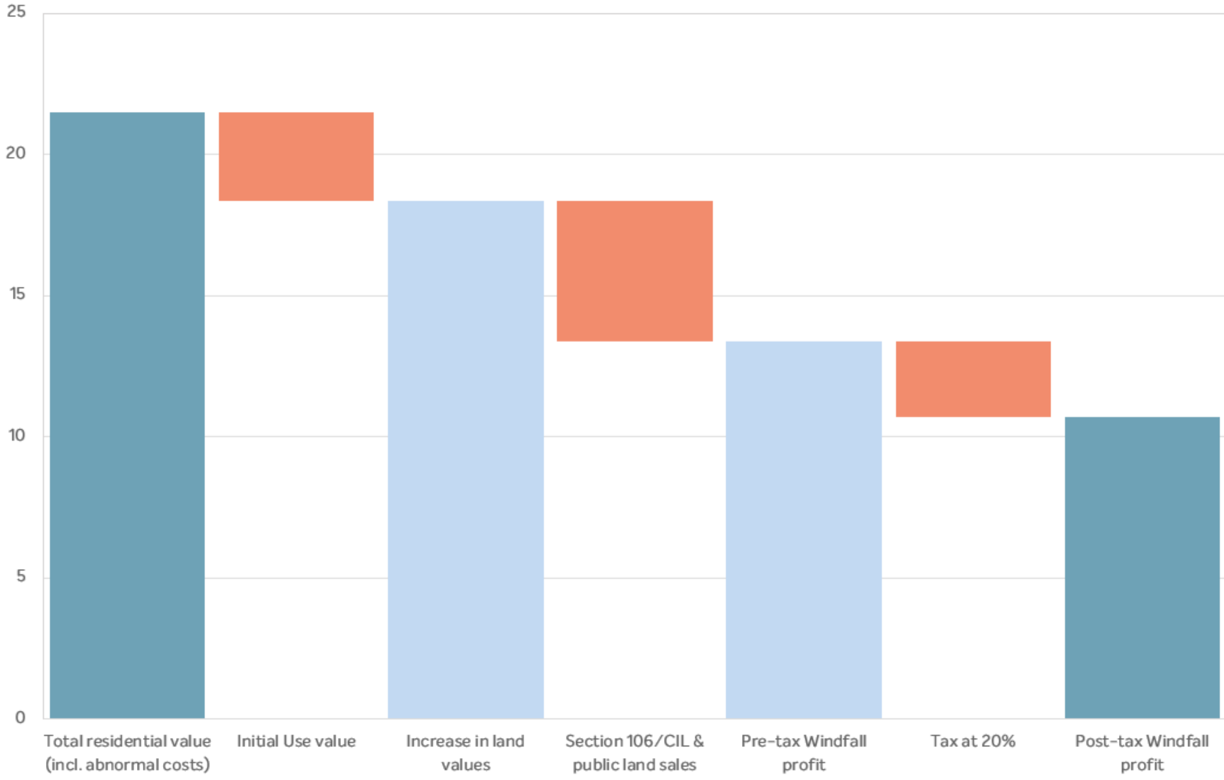
MHCLG provides data on the following data sets which form the foundation of the analysis.

- Estimates of the value per hectare of residential land by individual local authority. This assumes a 1-hectare area of regular shape and a net developable area of 80% of the gross area.
- Estimates of agricultural land and industrial land by LEP.
- Number of units built by local authority (table 253) adjusted so the totals equate to the new build completions in table 120.
- The density of housing per hectare of land including other spaces by individual local authority. The density data is derived by calculating the density of all residences in the hectare surrounding newly-created residential addresses, hence includes all open spaces, roads and other land required for place making. The density data therefore provides a net figure for the development of a given hectare of land.
- The proportion of new residential addresses created by previous land usage category by local authority to compute a more accurate use value estimate.

From these data sets the following can be determined:

- Number of hectares of land used for residential construction by local authority. All new builds constructed on previously developed residential land were removed from the analysis given that a planning permission award had already been granted. Total number of units – units constructed on previously developed residential land / density per hectare
- Total use value can then be estimated for each local authority by multiplying the number of hectares by the value of the underlying land. The computations are then summed to provide the use value by local authority, region and England. Industrial land values are used for previously developed land. Previously developed land with buildings that would be converted to residential to use are not included in these estimates as conversions for new dwellings are captured separately in table 120. For non-previously developed land agricultural land values are used with the exception of residential gardens. For residential gardens, discussions with market participants suggest that £50,000 per acre is a useful guide for valuation, although when much smaller parcels are bought and sold, the price might be higher. For the analysis we rounded up the £50,000 per acre to £125,000 per hectare to use a proxy. This only impacts 6% of new housing.
- Residential use value is estimated by multiplying the number of hectares by the residential land value.

Chart 3: Estimating windfall profits resulting from the jump in land values due to the granting of planning permission 2016/17 **(Source: MHCLG, Centre for Progressive Policy)**



Acknowledgements

The author would like to thank Professor Pat McAllister, Professor Tony Crook, Daniel Bentley, Dr Nicholas Falk, Charlotte Alldritt and John Dudding for their helpful comments and advice on the report, as well as the Centre's team of legal advisors. All errors are my own.