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Restoring the value of land: a new model for housing development

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Background

As reported in ACE's first paper into the housing market a potentially irrevocable housing gap (where the number of households outstrips houses built) is looming in the UK. Unless tackled this housing gap will see, at a conservative estimate, hundreds of thousands of extra people in the UK unable to own a home. The analysis in this report reveals that by 2021 the UK will have developed a housing gap of £185bn, the equivalent to 886,000 households. This growing housing gap, will add ever greater pressures to existing housing stock, as well as the ability of most to afford a deposit or access a mortgage. As such, the failure to tackle this housing gap through increased house building will not only remove the aspiration to own a house for most, but have massive widespread social and economic consequences for the UK's future.

This growing housing gap highlights an increasing disconnect between supply and demand as demonstrated by significant historic house price inflation. Such inflation shows that the market is not connecting supply and demand as a well functioning housing market should.

This disconnect between supply and demand has been further stretched by the financial crisis, which has subsequently changed the market dynamics of the housing sector for a number of reasons. These include amongst other things, the availability, access, cost and willingness of consumers and companies to take on credit. For this reason, the likelihood of heading towards future crises seems ever more likely, with the housing market not able to correct itself by properly aligning supply to demand.

Radical reform is therefore needed and, given the scale of the challenge, needs to be bold in its approach. Innovative thinking and policies are needed within the housing sector to address the ever-shrinking number of homes being built and the rift that has become apparent between supply and demand.

A good comparison to raise here is the seriousness that government has given to tackling the energy gap. The energy gap (the gap between energy generation and energy demand) was estimated by Ofgem to require a £200bn energy infrastructure investment by 2020 only one year shorter than the aforementioned housing gap.

Even though the housing gap will reach a similarly daunting £185bn, however, there are few signs from government of an increased focus, or a sophisticated or innovative response that seeks to increase the UK's house building to tackle the gap.

Abstract

This paper is the second in ACE's housing paper series and explores in detail the challenging conditions within the UK housing market.

Following the discovery of a £185bn housing gap and the disconnect between supply and demand in the housing market. This paper suggests an innovative model that attempts to address these challenges within the housing sector.

It proposes a Land Optimised Value Extraction (LOVE) model which is based around certainty and optimising the value which can be extracted from land by using principles such as a clear strategic direction, regulatory certainty and encouraging market competition.

This model therefore attempts to shift the emphasis and process of planning and development. This aims to reduce the burden throughout the system, reducing costs for parties involved, whilst also balancing the need for strategic housing development, commercial competition and local engagement.

Need for change

It is therefore time to open a new debate on the housing market, with the emphasis on developing a new way, a sustainable way, and a new model to solve these long established problems. A way that provides confidence, certainty, availability, affordability and importantly also attempts to over time slowly shift the market back towards to a reasonable rate of house price growth.

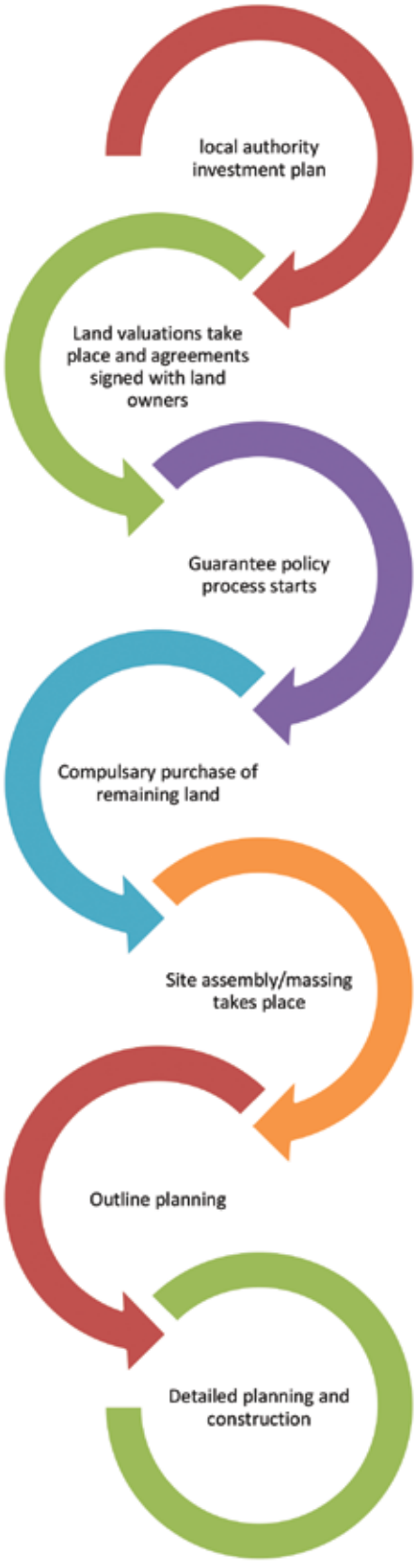
However, the solution is not just a short burst of building on a mass scale, as this would damage the asset value of those relying on them for retirement. As such the solution needs to be planned over the short, medium and long term so that house price inflation is brought under control gradually, and reflects the area in which the house is built. London's growth and demand, for example, is not an accurate reflection of the entire UK housing market.

This model will aim to

- Account for local conditions and needs by encouraging the local authority to engage with local residents as early in the process as possible.
- Extract the value created by government processes, such as the granting of planning permission.
- Provide a strategic plan for housing development, providing certainty and ensuring that housing is delivered in the medium and long run.
- Generate funds for local authorities to undertake not only infrastructure provision, but also to allow flexibility for them to undertake activity such as the preparation of brownfield sites to ensure development.
- Encourage efficient investment, minimising the need for lengthy negotiations, helping to remove some of the burden from developers.
- Clearly define the roles of local and central government, by ensuring local decision and spending powers, whilst also providing the support and guidance of central government.
- Minimise the fiscal impact on government, by creating a conducive environment for the private sector to operate.
- Continue to provide social and affordable housing, whilst also increasing overall housing provision to ensure sustainable future house price inflation.
- Encourage smaller developers to enter the market, and build more housing.
- Incentivise land owners to come forward with land for development.

Model outline

Land Optimised Value Extraction (LOVE)



- Covers 5 and 10 year periods with indication as to 20 year plan
- Provides certainty to market
- Allows local authority to plan investment according to local requirements
- Sites for development identified

- Encourage early engagement by paying a percentage of land value gain to land owner

- Only the movement in land value change is guarenteed reducing taxpayer exposure
- Local government using a central tool providing transparency and a clear picture to policy makers
- Limited impact on fiscal position of government balance sheet

- Land purchased at no more than market value
- Reduces the time and cost for the council of compulsary purchase procedures
- Puts emphasis on development at an early engagement

- Allows local authority to balance the needs of the local area for social housing, commercial, residential etc
- Local authority to address local concerns at site level reducing the liklihood of legal challenges later in process

- Developers engage and develop outline plans creating a competitive environment
- Developers bid at current market prices, creating the land value gain/loss.
- Cost to developers of challanges reduced by council at previous stage
- Winning bidder selected and money raised used to fund items outlined by council as part of investment plan
- Guarantee ends

- Undertaken by developer or delivery body and sale/ transfer of developed property to final party occurs

Model summary

Below is a proposed staging and structure under which such a policy could operate.

Local Authority investment plan

The first stage ensures that local authorities have in place strategic plans which outline areas where development is required in the medium to long term. Under these plans certainty is key, and support from the central government in the form of a guarantee on land value changes would only be available on the grounds of strictly adhered to timescales.

Government should not underestimate the certainty such plans can provide for local residents, investors and developers. As such, these plans should form the first stage of the local authority interacting with its local residents to derive an outline of where and how development should occur and at what pace.

Land sale agreements

The land sale agreements are an important part of this policy. They not only enable the local authority to capture the value of land over time but also provide an incentive for land owners to sell at the early stages of development. Land sale agreements would operate over the proposed five or ten year period.

In return for signing this agreement, the land owner will be entitled to a percentage of any gain in the land value over that period in addition to the agreed sale price. Importantly, if the price were to fall, land owners would still receive the value agreed upon in the original agreement. As this report has shown previously the risk of land values decreasing is relatively small and manageable and so this differential would be guaranteed by central government to support housing.

Importantly, this process allows an individual to engage early, and benefit from the process rather than go through the compulsory purchase system.

Site assembly and massing

Site assembly and massing is the process whereby a local authority would identify the types of development it expected within an area and sites for its development blueprint. This process is important as it starts to outline in more detail the preferred composition for potential developers, and builds local needs into the process.

Whilst this provides a guide as to the preferred composition of a development area and sites, however, it is important that it does not dictate a final solution that cannot be changed. The process is in place to provide further certainty and transparency as to how development is likely to occur, as part of the local authorities' strategic plan.

Giving local authorities some responsibility for an 'areas and sites master plan' should allow any significant objections and local concern to be dealt with prior to significant developer engagement. As such, the costs to developers of having to make changes and amendments to any plans should decrease. This not only encourages development but also means that there is certainty for the local authority as they have a greater degree of control over the output of a site.

Following the publication of the site assembly stage, the local authority would invite bids from the private sector to develop the site(s) with the private developer completing the outline planning phases for submission and final consent.

The private sector, whilst looking at the local authorities' plan for a site and area ultimately

has the expertise to determine profitability, viability, cost and sales potential. These factors will therefore determine how close the bids are to local authorities' blueprints. As such, these blueprints are guides to enable and drive private sector development whilst smoothing the process of planning, consultation, and development. These plans must therefore be based on commercial market drivers and not assume, for example, that a site could be developed with a unrealistic degree of social and low cost housing with simply private financing (such as 75% or 90%). This paper has explored in more detail how social housing would fit into the model proposed, and how commitments could be simplified in Appendix B.

By combining the expertise of the private sector and driving an area's development based on a long term and stable plan, the government and local authority should be able to plan and therefore develop more efficient services, meeting the needs of locals and reducing the likelihood of under or excessive provision.

Outline planning

The outline planning process would remain relatively unchanged and would continue to be driven by developers. This is important as developers bring skills to the process which local authorities would not have at their disposal in terms of commercial viability.

However, by bringing forward local authorities' involvement in the strategic purpose of the site, there should be minimal local objections and challenges at this stage of development.

Importantly as the model extracts changes in land value over time, and raises money for local authorities which can then be used for various means, the need for a timely and complex process of negotiating section 106 agreements, community infrastructure levy (CIL) etc. is no longer required. This shortens the time required for developers to form detailed pans, and removes a significant cost and burden for both parties.

Developers would be invited to submit plans (outline planning) up to 24 months before the transfer deadline. These plans would be evaluated by the local authority and compared to its original vision for the site and the value the developer places on the site accessed.

One party would then be selected under a competitive tender process to purchase and develop the land at the market value presented as part of the bid.

Sales complete and transfer point

Once the competitive tender process has taken place and a winning bidder is chosen, the transfer of the land (from the land owner to the developer) would take place.

The local authority and land owner would then benefit from the differential created by the original sale agreement, with the funds raised being spent on the purposes originally agreed.

Importantly this process has maintained the interest of the land owner, encouraged early engagement and has (depending upon price movements) provided the local authority with funds to spend on infrastructure, other sites, recreation etc.

Detailed planning and construction

Once the land transfer has taken place, the detailed planning process and development of the site would be undertaken as normal by the developer.

The detailed plan would include the final details of the development including items such as finalised details for accessibility of the site, land usage, car parks, landscaping, the position of trees, crime prevention measures, the final appearance of the development and the relationship of buildings to their surrounds.

Whilst a number of these issues will have been explored as part of the outline planning process and application in the developers bid, the detailed process puts in place the final specification for the chosen developer.

Construction of the site will then be undertaken by the chosen developer as normal.

Sale and transfer to final party

As with the current system, house builders and developers would still carry the sales risk, with units sold, rented or provided to housing associations or the local authority as agreed.

The fact that developers continue to carry this risk therefore needs to be recognised within the system. This is why it is important that developers continue to develop the detailed plan earlier in the process and place what they see as being a realistic commercial value on the site. This allows them to be adequately compensated and allow for pricing of sales risk.

It is also important to consider sales risk in relation to the time period of the policy. The further into the future a policy is undertaken the increased uncertainty there is and so the greater the risk premium has to be to cover this risk.

This would suggest that there may be an issue with a ten year policy. However, the ten year policy suggested in this paper does not need to undertake detailed designs until the later five year period, and so actual site numbers and requirements can be predicted more accurately. As such the ten year policy allows for certainty of development and the staggering of stages of development whilst not requiring additional risk to be priced into the equation.

The Land Optimised Value Extraction (LOVE) model for housing

This paper outlines a new innovative model which attempts to utilise a guarantee mechanism with a link to land values. This will encourage the release of development land for private developers and registered social landlord (RSLs) whilst also building certainty into models for strategic planning purposes.

The link to land prices is important for a number of reasons. Firstly, that land values continue to contribute to the value of an activity or site irrespective of usage. Secondly that this value can be used to ensure that policies reflect local conditions and it helps to ensure that any development occurs in a way which would not damage local house prices or social value. Finally, given the system and tools that are in place for monitoring and registering house prices (and land where sold) it should be relatively easy to implement a transparent system where local authorities could download land value data, providing accurate and historical information for policy formation.

This model would provide investible funds for local authorities for items such as infrastructure, land preparation, social projects etc.

Extracting land value is difficult, however, for the following reasons:

- Valuing property has to be done uniformly across the varied housing stock.
- What constitutes adding value to the land?
- Extracting value from homeowners is difficult as although they may be asset rich they can have limited liquidity.

It is important, therefore, to explore these in more detail before continuing. The valuation of a property will depend on its unique attributes and condition. As with any valuation that is based on human perception and expectation these values can vary. This variance, however, is no different to any other market or commodity, for example, car prices are based on their supply, desirability, features, performance etc. and overall demand conditions. Prices are determined by sellers, and buyers can choose to purchase at that price. The same mechanism occurs in the pricing of local properties with sellers comparing their property to local market conditions, getting a number of quotes and then setting their price accordingly. As such, the price of properties should be no less uniformly determined than in any other pricing mechanism.

Looking at the addition of value, the issue with extracting value is knowing what value has been added. Whilst planning permission does increase the asking price of a plot this increase in value is not realised if permission expires. As such any policy to extract value must have a clear process in place, with definitive stages defined over time to ensure development occurs. This therefore leaves the market with no doubt as to whether or not value is added to land as a result of government policies and the planning process.

The final difficulty is one of extracting a capital tax from those that may be income poor. This is an issue faced by proponents of policies such as the mansion tax. This is avoided in the model in this paper, as the value is only extracted over the life of the model as part of the transfer of

land ownership. As such, the funds are available and there are not issues with payment.

Looking at the development of new properties there are several stages where the market generally considers value to be added.

- The classification of land use allowing development.
- The completion or planning of infrastructure to support development.
- Planning permission for the development.
- Completion of building.

This raises the question as to who extracts the value at each of these stages, and what could be done to improve the provision of housing.

Given that the classification of land use and planning are artificial or regulatory inflators of price government should be able to extract value. That is to say that government controls these procedures, and thus when approving development is creating utility. If no procedures or development laws existed, the decision to build whilst not incurring any cost (e.g. application) would also not add any value. It therefore has to be asked if the cost of applying and undertaking procedures such as planning reflect the utility that is gained when permission is granted. For example, the decision to want to go to university adds no value to an individual's pay negotiations, whereas actually completing the course adds value.

Factors such as the completion of infrastructure whilst improving the value of a site, are slightly more complex in terms of increasing and extracting value given their cost and depending on the eventual party undertaking construction.

For example, section 106 agreements operate on the basis that they cover the cost of providing additional infrastructure. These agreements are seen by some, however, as being a tax on planning permission, that local authorities are trying to extract part of the value obtained by the granting of planning permission.

Whilst this rise in value is important, government can also play a role in proactively adding value to sites. For example, if a local authority proactively installs the infrastructure for a site it is done on the premise that the value of the site and its attractiveness to developers is increased and so offsets the cost of the investment.

The final significant step in value change is the completion of building. This adds value in so far as an individual pays for a final product and would generally not be prepared to pay that amount if the product was handed over incomplete. For example, buying a property off plan is generally cheaper than once constructed.

This therefore raises the questions as to how government can further increase house building looking at the concept of extracting and utilising this value chain to its greatest economic advantage.

However, it is important to realise that any value extracted from this process, unless improving a developer's prospects is likely to squeeze a developer's margins and so may reduce the prospect of house building.

Therefore the question to ask is how can government improve and optimise the value it creates within the planning process.

Changing values, assessing risk

If the house building process is to be kick started, using local price signals and relative values, it is important that government understands the degree of valuation changes over

time, and the potential risk of a policy mechanism in this area.

The data below from the Valuation Office Agency outlines the land values per hectare by current usage. As can be seen from the information there are significant variations in land values based on its status and usage. The value of agricultural land per hectare currently is between £13,000 and £17,000 depending on if the land is equipped with houses, cottages and farm buildings. Land used for industrial purposes increases significantly in value per hectare rising to approximately £900,000. By far the greatest value, however, is that of suburban land for residential development which currently is valued at approximately £2,000,000 per hectare.

	Average calculated from regions/area - £ hectare[1]
Value of equipped land with vacant possession[2]	£ 17,199.95
Value of unequipped land with vacant possession[3]	£ 12,926.44
Value of land for residential development	£ 2,086,481.48
Value of industrial land	£ 914,038.46

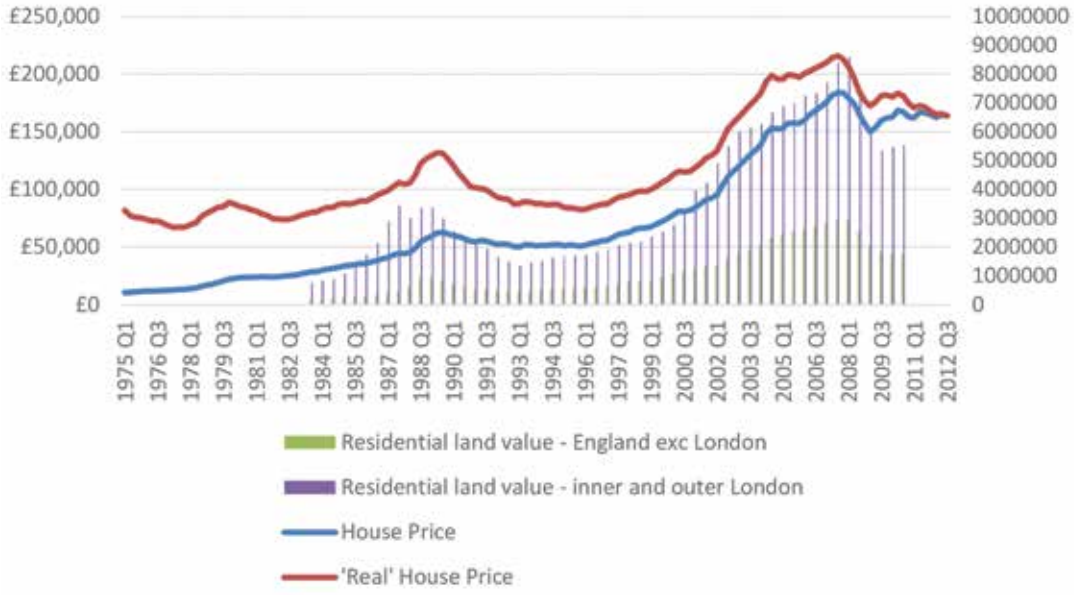
Source: Valuation Office Agency[4]

This indication that land value is gained as the use of land is changed. This is then further increased once housing development has taken place. However, it should also be noted that urban areas such as London could significantly influence this differential. This is because the value of properties in London is significantly above the rest of the UK.

It is therefore important to see how closely residential land value for development correlate to actual house prices both in and out of London.

Below, this report has plotted both real and nominal house prices against the residential development land prices5. As expected the data reveals that land values and both nominal and real house prices are positively correlated, with an R squared values of greater 90%. This means that the link between the data series (land values and property prices) is significant. As such if property prices had risen you would expect to see the same trend in land values and vice versa.

Residential land value and Nationwide house price and real house price data



Source: Nationwide and Homes and Communities Agency

This suggests that any benefit gained in value is maintained throughout the system. That is if land values rise in an area this rise is reflected in the property prices of houses within it. The value increase is captured in the new value.

This is important because if government wishes to target the value it adds from processes such as planning permission it needs to demonstrate that this value is embedded within the property value and does not simply disappear once the planning stage is complete.

There is, however, another issue to consider. The planning process, for example, does not occur over a short time period. It is therefore important that the potential risks are understood as to how much the value of a site can be affected whilst it is in the system. This is important because it not only provides certainty for government but also for any parties that would enter into an arrangement with government under its housing policy.

Analysis of valuation data over time

The following tables contain a summary of the analysis of the Valuation Office Agency data on land values. This analysis looks at how long it takes for land values to re-enter positive territory following its first (biannual) negative performance.

In England once the land value enters a negative period of growth the maximum time it takes on average to recover is 21 periods (biannual reporting) or just under eleven years. This therefore suggests that the maximum valuation exposure and risk of a policy based on changes in values is eleven years.

Whilst eleven years may seem like a long period most local authorities will have ten year investment plans, and more developed five year housing strategies. This should therefore allow for any worst case investment/policy scenario to be accounted for and controlled within their investment plan.

This report explores in further detail how this could be done within the outline of the more detailed land policy framework later in this document.

Looking at the average period in which value takes to recover, the analysis finds that the England average falls to three years. This average, however, takes into account the current recession. Given that this latest period of negative valuation growth has not gone through a complete cycle it is felt that this gives and unfair bias to the average. So if we look at the average prior to the current recessionary period it is found that the time taken to return to positive growth is five years. This risk is therefore much more inline with the period over which housing strategies are formulated at the local level and so could be managed.

Looking more specifically at the percentage of time land values spend decreasing and recovering their value, it is found that they are only performing negatively for 13% of the period. Policies that therefore use valuation change to help drive house building would therefore be considered less volatile than other forms of investment where the original capital sum invested is at risk.

For example, if you undertake the same analysis on the FTSE 100 index6 between 1984-2010 is found that the index performing negatively for 16% of the period. Thus performing slightly worse but not significantly different from land values. This small differential is not unexpected given the scale of the influence of the economic cycle on investments, shares and land values.

Data analysis – valuation changes

For entire dataset (Autumn 1983-Autumn 2010)

	Maximum period of loss where land value decreases		Average length of loss where land value decreases		Average length of loss when excluding the current recession/ crisis period		Current maximum length of loss of land value in current recession/ crisis		Total % of time where land values show negative return
Region	Periods	Years	Periods	Years	Periods	Years	Periods	Years	-
South West	22	11	7	3	12	6	4	2	13%
Eastern	24	12	7	4	10	5	5	3	15%
West Midlands	20	10	6	3	9	4	5	3	12%
East Midlands	22	11	6	3	10	5	6	3	12%
Yorkshire and the Humber	18	9	6	3	7	4	6	3	10%
North East	18	9	5	2	5	2	7	4	9%
North West	19	9.5	6	3	10	5	5	3	10%
South East	21	10.5	7	3	10	5	6	3	15%
England (excluding London)	20	10	7	3	11	5	5	3	12%
Inner and Outer London	26	13	10	5	16	8	5	3	20%
Overall average	21	11	7	3	10	5	5	3	13%

Whilst the analysis above, however, is useful in helping to determine policy periods (for example, five and/or ten years) the performance of the land value change must then be calculated over these periods, restricting values at the end of the pre-defined period to allow for detailed risk/reward analysis.

Looking at defined periods for housing policy

The results from the initial land valuation analysis suggest that there could be value in developing a mechanism to incentivise both land owners and local authorities to develop housing through the use of land values over different periods. This approach will extract the value that is created both over time and as part of procedures such as planning permission.

To do this a number of factors must be considered:

- What benefit there is to the land owner, and how this compares to the current options of selling land as required and under compulsory purchase?

- Would the process be simple for the local authority to implement, and how can the risks be limited?

- How development can be encouraged and the infrastructure improvements required for housing developments paid for?

- At what stage do items such as planning permission, local authority's plans etc occur and how would this align with the new system?

The first important question to answer is that of viability and the degree to which local authorities and land owners could be incentivised to develop and sell.

Exploring fixed term scenarios

Using the land value analysis mentioned previously reveals that the maximum time period for risk was eleven years, with the average time period risk at five years. For this reason this report therefore looks at two scenarios:

- If a local authority were to freeze the value of land what would the differential in its value be five years later?

- If a local authority were to freeze the value of land what would the differential in its value be ten years later?

In the analysis it is assumed that one hectare (unit) of land has its value frozen in each bi-annual period, for the defined periods mentioned above. This therefore would equate to two sites being developed in a year in total per region with an area of two hectares. However, this number could be multiplied by any integer to derive a desired scale of sites set aside for housing development.

The value of this land after the allotted period has expired (five or ten years) is compared to that when the land value was frozen and the performance measured.

This analysis was done for the period 1984 to 20107 to provide an ongoing analysis of how values would have changed and the potential exposure to risk.

Below are the results of this analysis:

Region	Valuation change for completed periods (last period Jan 2005)	Valuation change for completed periods (last period Mid 2000)
South West	£ 15,887,000	£ 28,647,000
Eastern	£ 27,078,000	£ 47,237,000
West Midlands	£ 17,347,000	£ 27,441,000
East Midlands	£ 14,712,000	£ 25,594,000
Yorkshire and Humber	£ 18,288,000	£ 26,771,000
North East	£ 18,121,000	£ 26,705,000
North West	£ 21,052,000	£ 30,889,000
South East	£ 22,943,000	£ 40,397,000
England (exc London)	£ 20,069,000	£ 32,708,000
Inner and Outer London	£ 48,266,500	£ 84,632,500
Overall average	£ 22,376,350	£ 37,102,150

The above table is encouraging as all of the regions would have made positive returns over the period 1984-2010 from a policy where agreements froze land values.

As suggested, however, by the previous analysis on the percentage of time land values are negative, there will be some period in which land values have fallen, and so value would be impossible to extract from the freeze in land value. As expected these negative period generally follow pre-recession peaks in land values.

Below is a table which shows the number of bi-annual periods8 in which the policy would have resulted in a negative return. Depending on the region and the latest available data there are 43 or 44 periods in total.

Region	Number of negative periods - 5yr	Number of negative periods - 10yr
South West	11	3
Eastern	13	4
West Midlands	9	1
East Midlands	9	2
Yorkshire and the Humber	8	0
North East	4	0
North West	8	0
South East	12	3
England (excluding London)	11	2
Inner and Outer London	15	8
Overall average	10	2.3

This data once again suggests that a policy which tries to capitalise and incentivise building based on land values would be possible.

Whilst in the ten year period the risks are small, the five year period does highlight that the risk of negative periods does increase. Therefore it is important to analyse whether policies should be distributed towards the medium or long term.

However, whilst the analysis of regional performance over time (where land values are measured if it had run 2 projects a year between 1984 and 2005 or 2000) is useful, it does not analyse individual performance or show the range of performance. Such information is important in assessing policy risks and returns.

The following table performs this analysis, and reveals that the over both the five and ten year periods the average price change across all regions is positive. This shows that on balance a policy involving land values would provide a contribution to local authorities and/or government if this value could be extracted.

Data analysis – valuation changes, fixed period scenarios

Data for 5 year fixed period scenario

Region	Percentage of time where land values show negative return (5 yr)	Percentage of fixed periods ending in negative return (5yr)	Average price change (5yr)	Poorest performance - price change (5 yr)	Best performance - price change (5 yr)	Average percentage price change (5yr)	Poorest performance in percentage (5 yr)	Best Performance in percentage (5 yr)
South West	24%	26%	£361,068	-£2,230,000	£1,130,000	69%	-100%	521%
Eastern	26%	30%	£615,409	-£1,207,000	£2,160,000	72%	-69%	410%
West Midlands	26%	20%	£394,250	-£590,000	£1,130,000	81%	-39%	424%
East Midlands	23%	20%	£334,364	-£950,000	£1,330,000	85%	-47%	455%
Yorkshire and the Humber	24%	18%	£415,636	-£970,000	£1,680,000	106%	-42%	406%
North East	22%	9%	£411,841	-£1,020,000	£1,920,000	103%	-46%	317%
North West	23%	18%	£478,455	-£980,000	£1,807,000	106%	-39%	365%
South East	26%	27%	£521,432	-£1,101,000	£1,463,000	64%	-65%	444%
England (excluding London)	24%	25%	£456,114	-£790,000	£1,440,000	74%	-52%	386%
Inner and Outer London	30%	34%	£1,096,966	-£1,948,000	£4,151,500	59%	-57%	303%
Overall average	25%	23%	£508,553.41	-£1,178,600.00	£1,821,150.00	82%	-55%	403%

Data for 10 year fixed period scenario

Region	Percentage of time where land values show negative return (10 yr)	Percentage of fixed periods ending in negative return (10yr)	Average price change (10yr)	Poorest performance - price change (10 yr)	Best performance - price change (10 yr)	Average percentage price change (10 yr)	Poorest performance in percentage (10 yr)	Best Performance in percentage (10 yr)
South West	20%	9%	£868,091	-£320,000	£1,962,000	148%	-26%	293%
Eastern	24%	12%	£1,389,324	-£680,000	£3,190,000	185%	-39%	486%
West Midlands	20%	3%	£807,088	-£12,000	£1,659,000	153%	-1%	256%
East Midlands	19%	6%	£752,765	-£162,000	£1,680,000	187%	-21%	375%
Yorkshire and the Humber	17%	0%	£787,382	£43,000	£1,978,000	192%	7%	350%
North East	15%	0%	£785,441	£15,000	£2,070,000	194%	3%	398%
North West	17%	0%	£908,500	£42,000	£2,235,000	212%	7%	442%
South East	24%	9%	£1,188,147	-£410,000	£2,690,000	150%	-23%	358%
England (excluding London)	20%	6%	£962,000	-£99,000	£2,229,000	172%	-11%	347%
Inner and Outer London	30%	24%	£2,489,191	-£1,367,000	£6,446,500	144%	-40%	349%
Overall average	21%	7%	£1,093,792.91	-£295,000.00	£2,613,950.00	174%	-14%	365%

For the five year period the average price change ranged from £334,364 in the East Midlands to £1,096,966 in London, with the average at £508,553.

This compares to the ten year period where the average price change ranged from £752,765 in the East Midlands to £2,489,191 in London, with an average of £1,093,792.

However, it is important to look at the range and the performance of the poorest periods to analyse risk. Looking at the five year period the poorest performance resulted in a £2,160,000 decrease in value, whereas over the ten year period the poorest performance resulted in a loss of £1,367,000.

The average performs better than this falling from a loss of £1,178,600 to £295,000. Whilst this demonstrates that there will still be risk with any land freeze policy it also shows the improvement between medium to longer term periods. Interestingly, the balance of lower risk as time increases would create an incentive for government and local authorities to plan longer term, thus also encouraging stability within the market.

The best performing periods and the probability of a good performance should also be mentioned in light of the risks mentioned previously. The best performing period over five years underwent a £4,151,500 increase in value whereas over ten years this was £6,446,500. The average performance of the best performing period increases from £1,821,150 over five years to £2,613,950 over ten years.

Importantly if you look at the range between the poorest performing and the best performing regions for both the five and ten year policy scenarios the range increases from £4,379,500 (5 year) to £6,142,500 (ten year). The rise in the range between the best and poorest performing regions is only 40% despite the time period doubling. This continues to demonstrate that whilst there is a greater degree of difference between the absolute values over the longer period, the relative risks have fallen, as the extremes of the policy have not increased by as much as the time period.

Whilst some of the results are not surprising, it is important that their scale is understood if a policy is to be created around land values. Vitally some of these results can help to drive the extent to which a local authority should tailor its housing policy to the medium and/or long term.

What mix of medium and long term policies should be implemented?

By calculating the potential benefit of land value changes over two defined periods, a ratio can be calculated between these periods to indicate where the balance of medium to long term policy definition should reside. This is important as it provides an evidence based approach to creating medium and long term policies, based on their benefits to the local area.

As can be seen from the table below the ratios vary between regions from 1.46 to 1.80. A ratio of one would indicate that the five and ten year periods resulted in the same return and so there was no differentiation between the two policy options. However, as this report has shown previously, the degree of risk of land valuations falling over the ten year period is lower than that of the five year period. As such, as this return of the ten year policy is above that of the five year policy the ratio increases (above 1).

Therefore the closer the ratio is to the five year period, the greater the rationale for policies to operate over a five year period rather than a longer period of ten years.

So for example, the North East under a 5 year policy linked to land values increases would see the income they generate increase to 1.47 times that amount over a ten year period. For the five year periods the policy would have generated £18,121,000 whereas for the ten year period this figure is £26,705,000.

This for example suggests that the North East would benefit from weighting their policies

towards that of the five year period, whilst running some ten year period schemes to provide longer term stability.

Whereas in inner and outer London the land value differential for the ten year is better (ratio 1.75), which suggests there is less benefit to having policies weighted towards the five year period. As such a more long term approach would remove risk whilst also continuing to provide a reasonable return.

Region	Ratio - comparison of land value gain for ten and five year cycles.
South West	1.80
Eastern	1.74
West Midlands	1.58
East Midlands	1.74
Yorkshire and the Humber	1.46
North East	1.47
North West	1.47
South East	1.76
England (excluding London)	1.63
Inner and Outer London	1.75
Overall average	1.64

These results suggest that the South West, Eastern, East Midlands and inner and outer London should shift their focus towards longer term policies. Whereas, areas such as the North East, Yorkshire and Humber and North West would benefit from having a more short term policy focus.

Again this analysis suggests that a policy linked to land values could not only be used but also tailored to create stable investment plans.

In addition to the tabular analysis above, Appendix A contains a graphical analysis of each region independently with the five and ten year policy periods highlighted by a yellow break line.

These graphical representations are useful to clearly show the risk periods. Also, given that data lags approximately two years behind current market conditions, they suggest that the risk of continued land devaluations falling within one of the periods suggested (five or ten years) for policy implementation, is reducing.

It is also important to remember that the current system is affected by land values, despite not actually being based around their movements. A recent report by the Department for Communities and Local Government (DCLG)9 revealed that changes to land and property values were seen as the two most important drivers of changes in the numbers of planning agreements negotiated. Importantly, the period covered in the report is 2007-8 when the financial crisis and recession had taken hold and yet 41% of respondents still felt that land value changes had a positive effect on the outcome of the negotiated agreement and 33% a negative effect. This demonstrates not only how resilient land values can be but also that they already have a profound effect on money raised.

Whilst the analysis above suggests that a policy based on land values is plausible, the question remains as to how government can effectively design such a policy.

This report will now explore how such a process could work. Within this, areas such as incentives to different parties, local needs, section 106 agreements, integration with the planning process and aspects such as social housing will be discussed.

Developing a new housing policy framework

The analysis performed to date, alongside the data from land values suggests that:

- A policy based around land values would be possible.
- That the risks of land value changes are manageable.
- That the policy should have a medium and long term option.
- A policy if developed correctly could use these funds to spur development.
- Policy should encourage efficient investment minimising the need for lengthy negotiations.
- Policy should also be supported centrally to help drive the overall degree of development.
- The balance of benefits and costs to local authorities and developers for the provision of infrastructure needs to be correct if they are to incentivise new housing.
- House building needs to be driven by local market conditions. Generally the most responsive house building markets have the greatest level of local policy involvement.

It is important that policies are effective in driving the correct behaviours, and are based on the economic conditions in which they operate. Housing development has traditionally been incentivised through a number of methods such as:

- Housing targets - these were part of regional plans and until recently were considered a practical way of driving development. In 201110, however, DCLG argued that these targets resulted in resistance in local areas, and were' all stick and no carrot' when considering development and local needs.
- Grants and support - these type of policies could be aimed at developers with regards to taking on less attractive sites, supporting affordable housing and even providing equity support for buyers. For example, schemes such as Homebuy, Help to Buy, Relocation Grant, Right to Buy and Homes for Heroes would all fit into this categories.
- Direct government spending - for example in the post war period and during the 1960-70s the government put significant money into the provision of social homes.

However, with the exception of direct government building these have not delivered the required housing supply and are not intrinsically linked to changes in economic performance.

Whilst government expenditure could be an option for increasing the supply of housing, given the UK's current fiscal position and the government's desire to deal with this is unlikely that direct investment will occur.

The policy this paper outlines is linked to land values. This has the benefit of reflecting local market conditions, and allows flexibility in the use of money raised. For example, local authorities would be able to split allocations across multiple service provision such as roads, rail, water, schools and health

Importantly, this policy has attempted to learn from previous government initiatives and devise a method of delivery that does not rely on a set outcome for house building by central government with little understanding of local market conditions and needs.

As the housing market approaches its true economic equilibrium the proposed policy's effectiveness falls. This thereby creating an automatic stabilising effect which does not over incentivise development.

Non incentivisation of housing occurs because, as the supply of housing increases, the value of land, and potential increase in value over time will fall. This provides less incentive for land owners to sell, and lower returns for local authorities from development.

This is important because the policy therefore does not encourage a 'pre-determined' outcome but instead constantly adjusts and incentivises the market to move towards equilibrium. This should therefore help to avoid housing bubbles and price collapses in future economic periods.

For example, the Building Societies Association11 (BSA), in June was reported as advising the government to put in place an exit strategy from its Help to Buy scheme, because without doing so it risked the danger of seriously distorting the housing market, and creating a future house price bubble.

This mechanism therefore provides the link between the supply and the demand side of the market, with building only encouraged if there is sufficient demand and so an upward pressure on prices. Therefore as highlighted in ACE's first paper trying to repair the disconnect that has been created to the balance of supply and demand.

Such a policy would be a radical step for the UK to undertake. However, if structured correctly a policy could provide a stable national framework, with local flexibility, encouraging development whilst reducing the cost to the public sector finances.

This structured approach is not dissimilar to that used in France and Germany where a central framework provides stability and consistency whilst local authorities are required to draw up development plans to tailor development to local needs. It is important to note that the power of these plans to ensure development comes from the fact that outside of the UK they are generally legally binding and provide certainty for developers.

The proposed policy has been developed to encourage local decision making and provide a policy lever that local authorities can use to implement long term strategic housing development plans.

These plans would therefore create the base line for housing development, and so would not replace land owners' and developers' ability to enter a partnership, apply for planning and develop a site outside of this strategic plan. This policy is not intended to drive the whole market for housing development but to ensure that development does occur where necessary. Importantly these plans encourage development that is in line with demand as the benefit to the local authority falls, as demand and supply reach a sustainable equilibrium, with socially acceptable price increases. Therefore both the private and public sector are incentivised to reach the market equilibrium and not a policy equilibrium.

Importantly this policy does not replace the role of the private sector in the delivery of housing but puts in place a framework to provide the certainty required to facilitate improved levels of investment.

By shifting the emphasis of policy towards the local authority the UK should be able to reduce the lengthy negotiations and planning objections which currently take place until a very late stage within the planning system.

Additionally, the policy also allows the local authority to benefit from the certainty it provides, and so contributing towards the cost of provision of items such as infrastructure. Across Europe there are various systems for the provision of such items with most having a degree of private provision and subsidisation from public funds. The model that is proposed in this paper benefits from linking the benefits of private funding for these provisions to market conditions. Thus it is in all stakeholder's benefit for the planning, development and scale of

housing to be reasonable and sustainable.

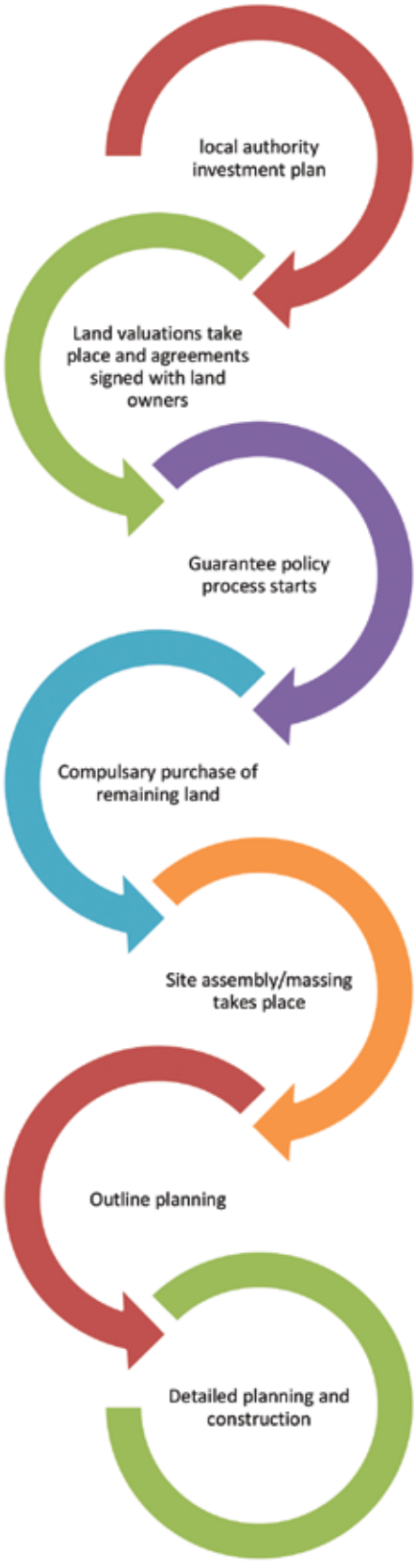
Below is a proposed staging and structure under which such a policy could operate.

- Local Authority investment plan.
- Land sale agreements.
- Interacting with different types of land owners.
- The guarantee.
- Site assembly/massing.
- Outline planning.
- Sales complete and transfer point.
- Detailed planning.
- Construction.
- Sale and transfer to final party.

To understand how each of these areas interact, this report will now explore the detail of each stage. In addition to the outline policy model provided opposite, appendix E and F also provide a more detailed proposal as to the timeline under which the model would operate.

Model outline

Land Optimised Value Extraction (LOVE)



- Covers 5 and 10 year periods with indication as to 20 year plan
- Provides certainty to market
- Allows local authority to plan investment according to local requirements
- Sites for development identified

- Encourage early engagement by paying a percentage of land value gain to land owner

- Only the movement in land value change is guarenteed reducing taxpayer exposure
- Local government using a central tool providing transparency and a clear picture to policy makers
- Limited impact on fiscal position of government balance sheet

- Land purchased at no more than market value
- Reduces the time and cost for the council of compulsary purchase procedures
- Puts emphasis on development at an early engagement

- Allows local authority to balance the needs of the local area for social housing, commercial, residential etc
- Local authority to address local concerns at site level reducing the liklihood of legal challenges later in process

- Developers engage and develop outline plans creating a competitive environment
- Developers bid at current market prices, creating the land value gain/loss.
- Cost to developers of challanges reduced by council at previous stage
- Winning bidder selected and money raised used to fund items outlined by council as part of investment plan
- Guarantee ends

- Undertaken by developer or delivery body and sale/ transfer of developed property to final party occurs

Local authority investment plan

The first stage of developing a new housing policy around the concept of extracting land values is to ensure that local authorities have in place strategic plans which outline areas where development is required in the medium to long term.

Most councils will already have a form of housing plan in place. These may not go into sufficient detail, however, as to identifying land for development within set stages, thus putting in place definitive timescales. As such these plans would need revising to reflect a new housing investment regime.

Under this regime certainty is key, and support from the central government in the form of a guarantee on land value changes would only be available on the grounds of strict adhered to timescales. This should not be a problem as there is mutual benefit to all parties involved in having the process run smoothly and quickly.

The interaction between a strategic central role and that of local authorities as a driver of development is important. For example in Germany there is a mixture of high level strategic plans which provide an overarching strategy and access to resource if required with local areas focusing on leading development in their area. Importantly, whilst there is an overarching macro housing policy it is important that decision making remains at a local level to encourage development. Forcing development onto a local authority will only serve to further exacerbate local opinions against future development.

Importantly, achieving the right policy balance would allow central government to have a much clearer picture of national housing development and demand, allowing them to adjust policy focus appropriately. This would provide local authorities with the necessary tools, processes and incentives to encourage development, whilst also allowing for specific goals for their area and sites which can be adapted to local needs. Finally, private developers and investors would be provided with certainty, an improvement in pipeline which should reduce the risk of costly delays and improve the efficiency of delivering developments.

Importantly, government should not underestimate the certainty such plans can provide for local residents, investors and developers. As such, these plans should form the first stage of the local authority interacting with its local residents to derive an outline of where and how development should occur and at what pace.

These plans by providing certainty, and strategic direction should also enable local authorities to drive efficiency in the development of housing and implementation of items such as Sustainable Urban Drainage (SUDs) and community schemes. This is because they are better equipped to integrate developments of all sizes into a larger system.

For example, the most efficient way to direct sewers, power grids and broadband lines and position items such as sub stations is to know where current and future development is going to occur. The UK's current ad hoc system of development and continued emphasis away from having a strategic direction therefore creates inefficiency and only helps to drive up the cost of even core infrastructure provision.

Further to this these plans would also allow local authorities to plan items such as schools and recreation activities with far greater degree of certainty thereby maximising the utility and coverage of these assets. This would maximise the social output and value of the properties provided within the area. Such aspects will be important as part of local residents willingness to engage in future development.

As such, as part of these plans, and under the new land value policy the emphasis is on early engagement. Currently planning and housing policies, whilst suggesting early engagement do not provide significant incentive to do so. There have always been cases of individuals holding up developments as they try to extract the maximum utility from their position or property.

Over time these plans would see the focus of the housing industry shift from its current position where there are concerns over planning regulations and section 106 negotiations, to a landscape of certainty where developers are able to focus on the sustainability and quality of delivery.

Given the proposed five and ten year policy periods proposed in this report, a local authority would have to update this plan every five years, outlining how it sees development occurring in the next five and ten year periods.

The current planning system

The UK planning system has developed over a significant period and connects into a wide variety of legislation such as building codes and standards, environmental laws, infrastructure provision etc. As such the system has never been thought of or designed as a holistic process that aims to achieve an ultimate outcome.

For this reason the government attempted to simplify and provide a framework for the planning system using the National Planning Policy Framework12 (NPPF). Given that this is still being implemented there is a limit to the extent to which this report can analyse its effectiveness to date.

The model in this paper therefore focuses on shifting the emphasis of planning forward, replicating other systems in Europe where decisions are made sooner providing certainty. As such, the planning system is not reformed as part of this report, but the way in which development is outlined, consultations undertaken, and finally outlined and detailed consent provided is discussed. The aim therefore is to build a supply side policy which attempts to innovate to ensure the UK housing supply in the is sufficient for future generations' needs.

Beyond this, however, there are specific policies which are discussed in more detail given their effect on the commercial viability of the site, and the degree to which they would change or be removed under the proposed policy.

Land sale agreements

The land sale agreements are an important part of this policy. They not only enable the local authority to capture the value of land over time but also provide an incentive for land owners to sell at the early stages of development.

This policy attempts to utilise the certainty gained in countries such as the Netherlands, where local authorities are directly involved in the purchase and sale of the land ready for development, whilst not actually requiring the local authority to take ownership.

Land sale agreements would operate over the proposed five or ten year period. Under this agreement an individual would agree to the transfer/sale of their land at current market prices to allow the process of planning permission etc. to take place, but with the actual transfer/sale being delayed until a pre specified date five or ten years into the future13. In return for signing this agreement, the land owner will be entitled to a percentage of any gain in the land value over that period in addition to the agreed sale price.

Importantly, if the price were to fall, land owners would still receive the value agreed upon in the original agreement14. As this report has shown previously the risk of land values decreasing is relatively small and manageable and so this differential would be guaranteed by central government to support housing.

The benefit of guaranteeing a negative movement in this way is that under the majority of scenarios where prices rise, central government would have no liability. Thus such a policy would have a much lower impact on the government's fiscal status.

Importantly, this process allows an individual to engage early, and benefit from the process rather than go through the compulsory purchase system. Application for land purchase agreements could run for a period of 6 or 12 months allowing an individual a fair and reasonable period to apply for a fair payment, which would compensate them for the sale of the land.

To make this process work efficiently, however, the compulsory purchase system also needs to be analysed in light of this new incentive.

Currently if a local authority does not already own the land, and it has gone through the process of identifying sites and engaging with developers or land owners unwilling to sell, they have to go through the process of compulsory purchase.

To do this they seek a compulsory purchase order (CPO), which will allow them to obtain land or property without the consent of the owner.

Within this, compensation can be paid for a number of items which include the value of the property itself, the cost of moving and even the cost of professional advice.

Whilst this is currently used as a last resort and is time consuming, it is felt that housing policy itself does not help to alleviate the pressure on CPOs and does not encourage individuals to avoid this process.

There are emotional attachments involved when it comes to compulsory purchase of land and individuals having to move.

By actively encouraging land owners to become involved with the local authority there is a sense of mutual benefit by being involved in the process early and having development and local improvement occur. Compulsory purchase could therefore be simplified to a deadline where market value is paid.

By providing the opportunity for land owners to sell and benefit from some of the increase in land value, whilst guaranteeing their agreed amount, a local authority would have demonstrated that it provided a fair system and incentive for early engagement.

As such, if an individual were to decide not to sell under this process and the last resort has to be taken by the local authority to issue a compulsory purchase order the price paid should therefore only reflect the market value. There would within this be provision for moving costs but the process would minimise compensation above the market value given that the land owner refused to engage with the previous system which is designed to provide an additional benefit to sale.

Currently CPO powers have to be used within three years, which fits within this report's proposed five year guarantee period whilst also allowing for some flexibility.

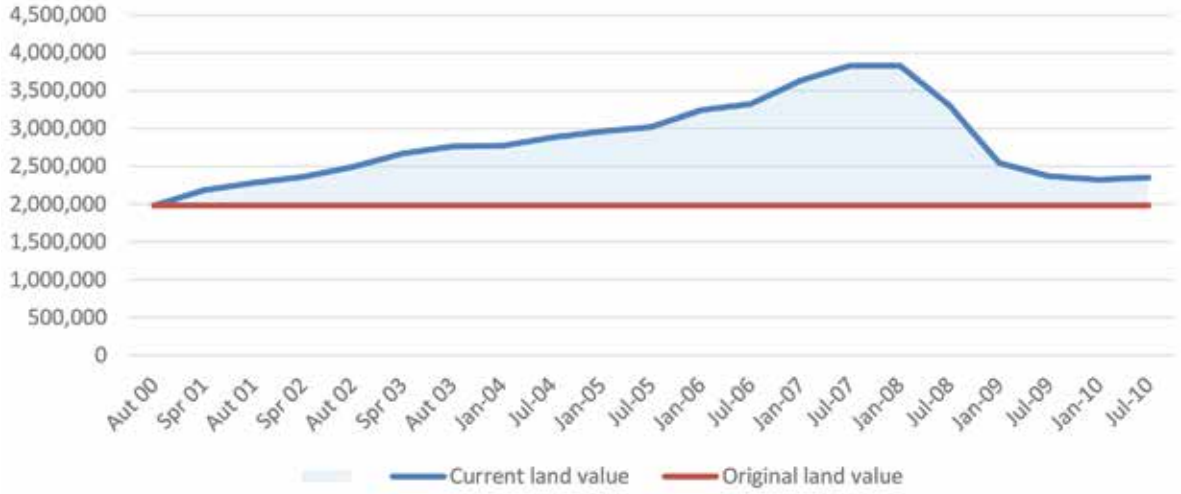
Whilst this seems to a blunt instrument, such systems to enforce development are used in other countries. For example, as discussed in the review of European Planning Systems report15 in Germany the public delivery body Gemeinde can designate land for urban development for housing and if necessary use CPO to ensure development goes ahead.

Looking more specifically at the guarantee, below are four graphs that show both a positive and negative outcome of the proposed five and ten year policies.

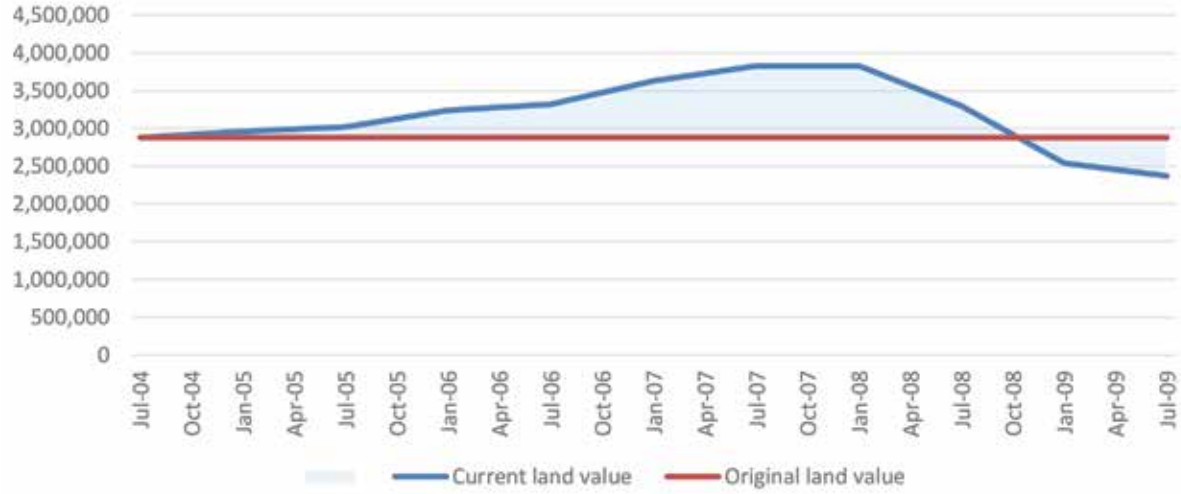
The area shaded in blue represents the change from the original agreed price, and so where positive, this would be the amount per hectare the local authority could allocate for various tasks. Whereas when negative, this area shows the extent to which the government guarantee would be liable per hectare to make up the original agreed sale price.

South East region - 5 year positive

South East region - 10 year positive



South East region - 5 year negative



South East region - 10 year negative

Whilst all four of these scenarios show varying degrees of benefit/loss it is important to remember that this report's previous analysis revealed that on average only 23% of five year periods and 7% of ten year periods ended with a negative return.

Where a positive return occurs, a percentage would go to the land owner for entering the scheme (e.g. 10%). The rest of the money raised, however, could be allocated for various tasks.

For example, the local authority could set a percentage rate to contribute to

- Infrastructure
- Social housing
- Schools
- Hospitals
- Preparation of brownfield land

Given that the local authority can decide where this money is spent and allocate a varying degree on any returns this policy creates an extremely flexible model.

This flexibility is important when considering the type of development that is taking place. For example, on an undeveloped site that was previously farmland, a larger percentage of the money would be allocated to providing infrastructure, as this is not already in place. Alternatively in a town or city where a brownfield site was being developed the land may have a degree of clearance and decontamination to be removed to encourage developers to bid for the site following the guarantee period. For example, Appendix A considers the use of the land value differentiation to enable site preparation for smaller developers.

This raises the question of ownership and liability. Under the policy the private land owner would still legally be in charge of the land, however, they would have agreed a sale date. As such, the local authority may need to agree to compensate the individual for any maintenance that is required in the interim period.

There will be circumstances where the local authority may need to take a more active role. For example, for brownfield development, the local authority would be required to put in place within the agreements a clause whereby it takes over the liabilities related to the land, site works and its maintenance whilst it was prepared and decontaminated for development.

In the case of brownfield sites such preparation works would be paid for using the money raised at the point of sale to the developer.

Importantly during the guarantee period the planning process would continue to ensure that by the five year deadline the land was ready for transfer/sale to the developer.

This policy therefore provides a tool to bolster a local authority's plans, shifting the balance of the UK housing sector by enabling local authorities to extend their reach from one of only allocating land under the UK planning system to one of consultation, and encouraging the provision of land.

Master planning - Site assembly and massing

Site assembly and massing is the process whereby a local authority would identify the types of development it expected within an area and sites for its development blueprint. They might include residential low rise, residential high rise, commercial, retail, social housing or schools.

This process is important as it starts to outline in more detail the preferred composition for potential developers, and builds local needs into the process.

A local authority detailing such aspects is not a new concept and is undertaken in countries such as the Netherlands and Spain as part of local plans to drive housing development. In the latter for example, the development plan includes provisions on density, building type and environmental and sustainable requirements. This provides clarity and certainty to developers as to the needs of local residents and the local authority.

Whilst this provides a guide as to the preferred composition of a development area and sites, however, it is important that it does not dictate a final solution that cannot be changed. The process is in place to provide further certainty and transparency as to how development is likely to occur, as part of the local authorities strategic plan.

Traditionally the process of developing a site and submitting final plans to the local authority would have been undertaken by the developer and land owner. In addition, the interests of the land owner in the site was maintained by maximising the price they are paid by the developer on approval of the plans.

By placing all the emphasis on planning the development onto these private parties there is a significant probability of lengthy appeals and planning procedures to get developments approved.

Giving local authorities some responsibility for an 'areas and sites master plan' should allow any significant objections and local concern to be dealt with prior to significant developer engagement. As such, the costs to developers of having to make changes and amendments to any plans should decrease. This not only encourages development but also means that there is certainty for the local authority as they have a greater degree of control over the output of a site.

Under the new regime certainty, flexibility and the responsiveness of a site to local needs is encouraged earlier in the process to avoid delays. This is not only to speed up development, but should also help to reduce the cost and time taken to apply for final site planning permissions. Having the local authority pre-define handover dates to access a central government guarantee scheme also ensures that the 5 year policy deadline is met.

The new model therefore recognises that there is still a need to keep landowners involved in the process of sale, planning and approval which is why the guarantee provides them with a clear outline of their risks and potential return. However, it also attempts to address the issue of local authority being able to better support developers in approving developments.

As mentioned previously this site massing and assembly stage whilst providing an outline blueprint to support the Local authority's strategic plan would not be a static final development and planning proposal.

Following the publication of the site assembly stage, the local authority would invite bids from the private sector to develop the site(s) with the private developer completing the outline planning phases for submission and final consent.

These plans would then be approved by the local authority based on which developer submitted the best mix and proposal given the local authorities proposed blueprint and long term development goals.

Getting this balance between local authorities being able to develop strategic plans to meet future housing needs while being able to use private expertise is important.

The private sector, whilst looking at the local authorities plan for a site and area ultimately has the expertise to determine profitability, viability, cost and sales potential. These factors will therefore determine how close the bids are to local authorities' blueprints. As such, these blueprints are guides to enable and drive private sector development whilst smoothing the process of planning, consultation, and development. These plans must therefore be based on commercial market drivers and not assume, for example, that a site could be developed with a unrealistic degree of social and low cost housing with simply private financing (such as 75% or 90%). This paper has explored in more detail how social housing would fit into the model proposed, and how commitments could be simplified in Appendix B.

By combining the expertise of the private sector and driving an area's development based on a long term and stable plan, the government and local authority should be able to plan and therefore develop more efficient services meeting the needs of locals and reducing the likelihood of under or excessive provision.

Within this development local authorities will have the responsibility of balancing their social needs with that of private housing and the ability of the developers to make a profit out of the site. It is not in local authorities' interest to plan a site that no developer is willing to purchase and develop, just as it is also not in their interest just to allow sites to be developed in a densely populated manner maximising profit but lowering the areas overall desirability.

Outline planning

The outline planning process would remain relatively unchanged and would continue to be driven by developers. This is important as developers bring skills to the process which local authorities would not have at their disposal in terms of commercial viability.

Having created a process, however, whereby the concept of a blueprint, planning sites and addressing local concerns is brought forward prior to the outline planning stage, local authorities are able to create longer term plans whilst also reducing the likelihood of costs escalating for developers due to the planning and appeals process.

Importantly as the policy extracts changes in land value over time, and raises money for local authorities which can then be used for various means, the need for a timely process of negotiating section 106 agreements, community infrastructure levy (CIL) etc. is no longer required. This shortens the time required for developers to form detailed pans, and removes a significant cost and burden for both parties.

Developers would be invited to submit plans (outline planning) up to 24 months before the transfer deadline. These plans would be evaluated by the local authority and compared to its original vision for the site and the value the developer places on the site accessed.

One party would then be selected under a competitive tender process to purchase and develop the land at the market value presented as part of the bid.

This competitive process would encourage efficiency whilst maintaining a sense of direction by the local authority's strategic plan. Whilst local authorities have an incentive to ensure that the economic and social value placed on the site is as large as possible (due to the extraction of the differential in value), developers have the counter incentive to minimise the valuation to make as much profit as possible for the sale of the properties. Whilst both these incentives exist, however, the competitive process encourages both parties not to differ greatly from the median/market value as it is unlikely to be successful in the bidding process.

The process of tender can also be used to encourage a strong focus on starting to build as soon as the transfer has taken place, as the lead time between bidding, building, and selling properties, would be significantly shorter - reducing risk. Local authorities would therefore be in a position to incorporate measures in their bidding process to ensure development starts in a timely manner.

It is therefore important that the local authority has achieved the right balance of providing a strategic framework and outline as to how they wish development to occur and allow enough flexibility for developers to submit varying plans to meet the local authority goals, allow innovation and provide a degree of choice as to how development will occur.

Importantly this process does not preclude the possibility of housing associations bidding for sites alongside private developers, thus providing enhanced competition and potentially a wider variety of options for the local authority.

Whilst competition should provide an efficient pricing mechanism, if instances do occur where competition does not result in a fully effective price and disputes could occur, government may wish to explore establishing an independent process which could take a view on if the level of pricing is correct.

Sales completion and transfer point

Once the competitive tender process has taken place and a winning bidder is chosen, the transfer of the land (from the land owner to the developer) would take place.

The local authority and land owner would then benefit from the differential created by the original sale agreement, with the funds raised being spent on the purposes originally agreed.

Importantly this process has maintained the interest of the land owner, encouraged early engagement and has (depending upon price movements) provided the local authority with funds to spend on infrastructure, other sites, recreation etc.

Importantly under the agreement, if the value of the land has fallen, the land owner is guaranteed the original agreed price with the government guarantee providing the bridge between the current value (paid by the developer) and the agreed value.

Detailed planning and construction

Once the land transfer has taken place the detailed planning process and development of the site would be undertaken as normal by the developer.

The detailed plan would include the final details of the development including items such as finalised details for accessibility of the site, land usage, car parks, landscaping, the position of trees, crime prevention measures, the final appearance of the development and the relationship of buildings to their surrounds.

Whilst a number of these issues will have to have been explored and an outline provided as to the developers intent during the bid, and outline planning stage, the detailed process puts in place the final specification for the chosen developer.

By pushing forward the discussion process, and the need for local authorities, developers

Current obligations - section 106 and the Community Infrastructure Levy (CIL)

Section 106 agreements are used as part of the planning process and requires developers to help offset and pay for improvements given the effects of development. These legal agreements between the local authority and developer are negotiated on a case-by-case basis and can outline a number of obligations for the developer that must be undertaken as part of the proviso of being granted planning permission.

For example, Kensington and Chelsea's planning obligations publication16 outlines how Section 106 obligations can:

"(i) restrict the development or use of land in any specified way; (ii) require specified operations or activities to be carried out in, on, under or over the land; (iii) require the land to be used in any specified way; or (iv) require a sum or sums to be paid to the local authority (or the Greater London Authority) on a specified date or dates or periodically."

These agreements hold considerable weight as any agreement is required to be in place before planning approval is granted, and so before development can occur.

Such agreements are not always easy and cheap to negotiate, however, and the requirements of local authorities can considerably impact on the potential profitability of a scheme.

The government therefore launched a review of planning obligations (please find more detail in Appendix C), and in August 2012 a consultation was issued on renegotiating Section 106 agreements with a view to improving the possibility of development.

The Community Infrastructure Levy (CIL) is not mandatory for every area, with the local charging authority17 deciding if they wish to levy such a charge on development.

In terms of the likely types of developments that charge covers, these would be considered buildings which are used and accessed. So for example, buildings which are accessed purely for maintenance purposes would not be covered by CIL.

The CIL is calculated in pounds per square metre of gross floor space but developments are able to change the use of areas and account for demolition within the calculation, and there is a lower limit of 100m^2 which can exempt smaller schemes.

Importantly, the charge is levied at the commencement of development, but can also be paid through instalments.

Money raised through the levy is then invested into infrastructure improvements in the wider area, with the local authority required to produce a report which details any monies raised and what investment took place as a result of this income.

The community infrastructure levy, by operating as a tariff, was intended to make the process of negotiating contributions towards infrastructure simpler and cheaper to implement, thus speeding up development. This over time should increase the contribution from smaller developments where section 106 agreements may not have been negotiated in the past.

The aim of this system was that whist section 106 would pay for site specific infrastructure improvements to social housing etc. the CIL would fund infrastructure that was not site specific.

The interactions between these obligations is not simple, and whilst CIL aims to simplify some of the negative aspects of individual site by site negotiations, the resulting system is complex and therefore is likely to put off investors and developers without a detail understanding of the sector.

and local people to agree on a winning bidder, a greater number of the important decisions have been made within the outline planning phase.

This model therefore aims to achieve a more efficient, faster and greater balance between the cost, competition and forward planning of development by all parties.

Sale and transfer to final parties (homeowners)

As with the current system, house builders and developers would still carry the sales risk, with units sold, rented or provided to housing associations or the local authority as agreed.

The fact that developers continue to carry this risk therefore needs to be recognised within the system. This is why it is important that developers continue to develop the detailed plan earlier in the process and place what they see as being a realistic commercial value on the site. This allows them to be adequately compensated and allow for pricing of sales risk.

It is also important to consider sales risk in relation to the time period of the policy. The further into the future a policy is undertaken the increased uncertainty there is and so the greater the risk premium has to be to cover this risk.

This would suggest that there may be an issue with a ten year policy. However, the ten year policy suggested in this paper does not need to undertake detailed designs until the later parts of the policy period, and so actual site numbers and requirements can be adjusted. As such the ten year policy allows for certainty of development and the staggering of stages of development whilst not requiring additional risk to be priced into the equation.

Conclusion

The policy outlined in this paper has been designed to allow the UK to create a long term sustainable model for housing development. Such innovative thinking will be required if the UK is to fill the looming housing gap and supply shortages that are forecast.

The Land Optimisation Value Extraction model attempts to utilise increased land values created by government whilst also encouraging early engagement, private developer participation, encourage competition, embed certainty whilst also minimising the cost to the public sector.

The timing of the model has been primarily designed to provide certainty to the market, encouraging sustainable house building that drives the market towards its economic equilibrium.

Alongside this, the lead in time until the model taken effect would not only allow for government to consult on and finalise the details of a new housing framework, but also coincides with the recent announcement of a total of over £5.1 billion of investment to support housing in England between 2015-16 and 2017-18. Including £3.3 billion of new funding for affordable housing between 2015-16 and 2017-18.

Such action could therefore provide the housing sector with the incentives and certainty required to build the resilient housing stock required to support not only the current generation but future generations to come.

Appendix

APPENDIX A

Enabling small scale development

One of the issues with the current housing system is that its complexity and cost favours larger developers. The economies of scale and expertise they can employ compared to SMEs make them difficult to match when developing a site.

In many towns and cities, however, small scale sites which could be developed with possibly up to 10 houses are underutilised. These sites are likely to be located on old retail or commercial sites alongside roads and railways etc.

The costs and risks therefore attached to the site when considering items such as land contamination. can be high relative to the eventual sale price.

The system we have proposed would allow the local authority to build up a pool of small sites within its plan and utilise the land value change to prepare the site for development.

To do this efficiently, local authorities are likely to need the skills and scale of a larger development company for site preparation. A contract for a developer to undertake such works across the area on the sites they identify would not only provide sites that could then be tendered to local developers, but also provides diversity for larger developer portfolios.

This removes a lot of the burden from smaller developers and allows them to concentrate on the outline planning and construction of the project knowing that site preparation risks have been accounted for.

The financial crisis and recession has made it more difficult for such developers to raise funds to build projects. There is no point in the local authority preparing and having 50 sites ready for development if finance can't be raised to get construction underway on the site.

Whilst pre-preparation of the site, however, has reduced the risk to small developers and so increased the likelihood of finance being available, there still may be issues with the raising of finance.

The issue should no longer focus around the cost of finance and the potential profit of the site, because previous obligations on the developer such as section 106 and CIL are no longer applicable improving profitability. Also, as the land value mechanism is designed to reflect economic conditions and encourage the market back to equilibrium subsidising finance would not be a step that was necessary.

This therefore concentrates policy on the availability of capital. This capital could be made available by government, up to a predetermined amount, at the same rate as a commercial loan to ensure development whilst finance conditions remain tight.

These loans should not only help to open up smaller scale developments but will also provide the local authority with a further return on development.

APPENDIX B

Integrating social housing

Social and affordable housing provision as discussed earlier constitutes the main area of negotiation within Section 106 agreements.

Given ACE's first paper revealed a housing gap of £185bn and equivalent 886,000 homes there is a significant constraint being put on affordability and the need to bolster house building, it is also important that the provision of social and affordable housing is built into the proposed new model.

As discussed earlier within the context of S106 agreements, social housing and affordable housing does have cost and site viability implications for housing development. The key aim of the mechanism built into this model is therefore to simplify the process surrounding the provision of social housing, reduce the cost of any negotiations that do take place, and encourage sufficient sustainable house building

For this reason it is important to understand current affordable housing provision. In 2010-11 approximately 39,000 homes were provided under the category of social rent. Social rented housing is owned by local authorities or privately registered providers (such as housing associations), and provides rental rates to eligible households under a regulated framework. This number would therefore include the majority of the approximately 32,000 permanent dwellings completed by Housing Associations.

Intermediate rented affordable housing provision accounted for approximately 4,500 homes and includes schemes such as shared equity (shared ownership and equity loans), other low cost homes for sale and intermediate rent, but not affordable rented housing. Finally approximately 17,000 low cost home ownership houses were provided. Given that these homes would not be under the control of the local authority or housing association they would therefore have to be counted within the private enterprise numbers of completed dwellings.

As such, we can infer that from the 140,000 permanent dwellings completed in 2011, that approximately 35,000 of these were provided by housing associations and local authorities (25%), and approximately 25,000 (17%) by private market.

Alongside the data above it is also useful to make some international comparisons. For example, in France the 2003 Urban Renewal and Solidarity Act makes use of planning instruments to implement a 20% affordable housing norm for both new and existing areas, accompanied by a fine and reward system for local authorities that is dependent on their compliance with the Act.18 In Spain 5-15% of land is simply handed to the local authority, which can then be used to supply houses at lower than market rates.

Given that the model proposed in this paper removes the need for Section 106 agreements and the CIL, it has already reduced the commitments that previously had the potential to make sites unviable for developers, encouraging building.

It is therefore important that such costs are not just transferred to another commitment such as social housing, thus continuing to act as a disincentive.

Having said this there are areas of the UK such as London where the need for affordable housing is significant, and the potential gains that can be made from development are substantial.

The proposed model in this paper recognises it therefore has to allow flexibility to negotiate additional social housing provision.

Finally, there are also smaller sites (for example, developments below ten units) where enforcing social housing provision would make development unviable and unprofitable. This has been one of the criticisms of the CIL mechanism.

As such, the this paper proposes that the government explores in more detail a lower limit whereby sites would not be required to provide social housing provision. Above this point, developers would be required to provide 15% of the total developments square footage to social housing.

This is below the current 17% provision that was calculated above, below the 20% provision in France and in line with the higher end of provision in Spain.

Given that Section 106 agreements and CIL will no longer be used as mechanisms to extract funds from developers, however, thereby reducing their financial commitments, that a standardised process and provision is vital to allow for additional and reasonable allowance of extra social housing provision if required.

The social/affordable mechanism as part of this model would therefore allow a local authority to negotiate a discounted price (15% below market value) on a further 15% of the development, which it could pay for using funds raised from land value changes.

This would make the total and maximum potential provision 30% as some developments have aimed for in London. However, it is important to emphasise that the extra 15% provision is to be agreed between the developer and the local authority and can be refused by either party without affecting the approval of development.

It is important to remember that the provisions mentioned above refer to private development that is only part of the strategic plan.

Outside of the strategic plan, private development would not require any units to be given as social/low cost housing. This places an emphasis on local authorities to ensure their strategic plans were realistic in there assumptions both in the short, medium and long term as well as economically and socially viable.

In addition, it is also important to note that under the proposed model, housing associations can compete for sites identified within the strategic plan alongside private developers, whereby a significantly larger degree of social/low cost housing would be provided.

This social and low cost provision framework therefore creates:

- A simple basic rate of social and low cost provision within strategic plans with no negotiation costs.
- Flexibility in provision above and beyond the 15% rate if negotiated between the parties.
- Encouragement of small site development.
- Allow private development outside of the strategic plans by removing commitments on developers
- The ability for housing associations to operate both within and outside of the land value mechanism

APPENDIX C

The scale, complexity and negotiation of obligations

A recent report by the Department of Communities and Local Government (DCLG)19 lists the obligations covered in their analysis of planning obligation. As can be seen from the list below there are a substantial number of items for both developers and local authorities to consider and negotiate.

Whilst each of these items on their own may not come at considerable cost, or take a significant period to negotiate government, the cumulative effect such items has on housing development must be considered.

Affordable housing - On-Site provision

Affordable housing - Off-site provision

Affordable housing - On-site provision of land only

Affordable housing - Off-site provision of free or discounted land only.

Affordable housing - Commuted

Provision of open space either within a development or via a direct payment to the LA.

General environmental improvements including landscaping

Ecology and nature conservation, countryside management and community forests

Allotments

Sport facilities: sports fields, club houses

Pollution and Waste Management

Archaeology

Maintenance of open space

Traffic/highway works, temporary or permanent

Traffic management/calming

Parking: management or parking restrictions, car restrictions and car free areas provision of parking areas

Green transport/travel plans

Public and local transport improvements

Pedestrian crossings, pedestrianisation, street lighting

Provision or improvement of footpaths or pathways

Cycle routes, management, safety

Community centres: construction, funding, improvement

Community/cultural/public art

Town centre improvement/management

Library, museum and theatre works/funding

Childcare/crèche facilities, provision and funding

Public toilets

General Community Facilities

Health services: community healthcare, construction of surgeries

CCTV and security measures

Waste and recycling facilities

Religious worship facilities

Employment and training

Local regeneration initiatives

Physical development or funding for education at all levels; nursery, primary, secondary schools, higher education facilities

General development restrictions

Administration and/or legal fees for S106 negotiations

S106 monitoring fees

Other

Over time the number of arrangements has been increasing with the value of obligations secured in 2007-08 worth £4.9bn of which approximately half is for new affordable housing. This was an increase on the £4bn negotiated in the previously analysed period of 2005-6.

Looking at the breakdown of the obligations agreed in England the following is revealed:

- £2.6bn was for affordable housing
- £235m was for open space
- £462m was for transport and travel
- £192m was for community and leisure facilities
- £271m was for education
- £183m was for other obligations
- £16m was for obligations entered into directly with county councils related to waste and minerals permissions
- £900m was for land contributions for uses other than for affordable housing

This distribution of the funds raised reveals that the majority is used for social housing and not infrastructure investment. Whilst the £4.9bn raised is important for local authorities, one has to question the efficiency of how this is raised given all the time that goes into negotiating these agreements.

Interestingly, the DCLG report also reveals that local authorities are losing specialist staff that work on Section 106 agreements because part of the negotiated sum from the agreement pays for the cost associated with administering planning agreements.

The recent government consultation on Section 106 agreements explores how activity has fallen because agreements negotiated prior to the recession and financial crisis as they are now seen as being too expensive and onerous on developers given current market conditions.

The recommendation is therefore to renegotiate such agreements. This could be a difficult task, however, given that the expertise to negotiate these agreements is being lost due to lack of funds raised from the signed/completed agreements.

Another concern is that monitoring of delivery is less developed than the negotiation of the agreements. As with all policies and systems implemented by government such as taxation ensuring compliance and delivery is key to efficiency. The more complex the system and agreement the more likely it is that full delivery and efficiency will be reduced.

Although local authorities must make a judgement on economic viability considering the requirements of the cost of complying with the Section 106 agreements and other policies such as CIL, such judgements are made difficult given all the policy levers have not been developed holistically.

Therefore, given the diversity of the requirements of local authorities, the complexity and time taken to negotiate and the confusing interaction between various systems it is not surprising that development is not incentivised.

APPENDIX D

Example of other obligations

Section 278 (Highway Act)

For example, section 278 (Highway Act) is a legally binding document to ensure that the work to be carried out on the highway is completed to the standards and satisfaction of the local highway authority. The agreement allows for improvements to the road network as a result of the impact of the sites development, with the developer paying a commuted sum to the authority upon completion, which covers maintenance for a pre-determined period. Within this negotiated agreement the full costs are usually paid for by the developer, as well as other aspects such as administration and legal inspection costs.

Sustainable Urban Drainage

Then there are also items such as Sustainable Urban Drainage (SUDs), these systems are expected to be put in place by developers on site to create relief mechanisms that simulate the natural environment in the management of water. This therefore reduces the risk of more serious issues such as flooding.

Currently SUDs are required to be implemented into sites, but depending on the site size and features there are varying degree as to how far they can be implemented. Generally, the bigger the site the more likely it is to achieve a full solution.

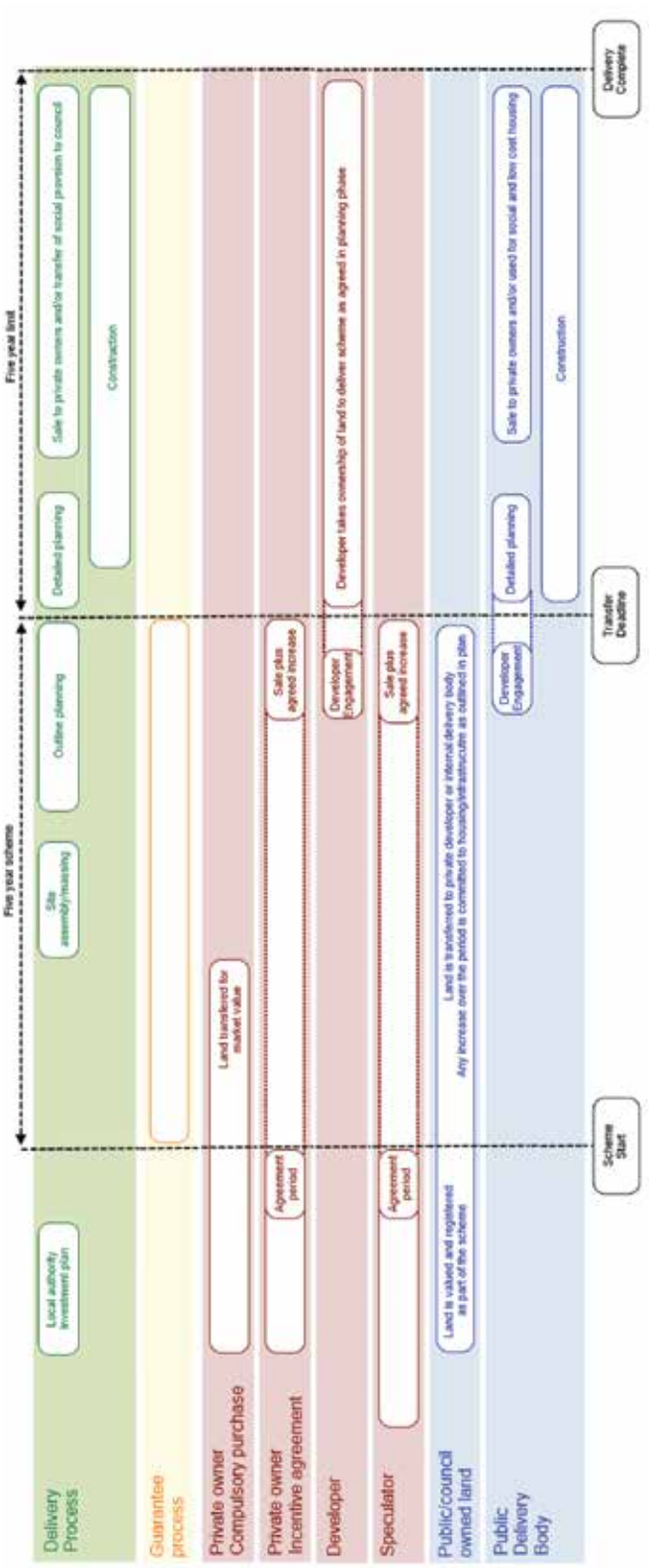
National guidance on SUDs is due from government but currently some local authorities have taken the initiative and produced their own SUDs guidance, for example, Oxfordshire county council.

Importantly, whilst SUDs do provide a step towards better management of water, currently the cost of implementation falls to the developer. This adds another obligation on them with regards to developing sites.

APPENDIX E

Illustrative schematic

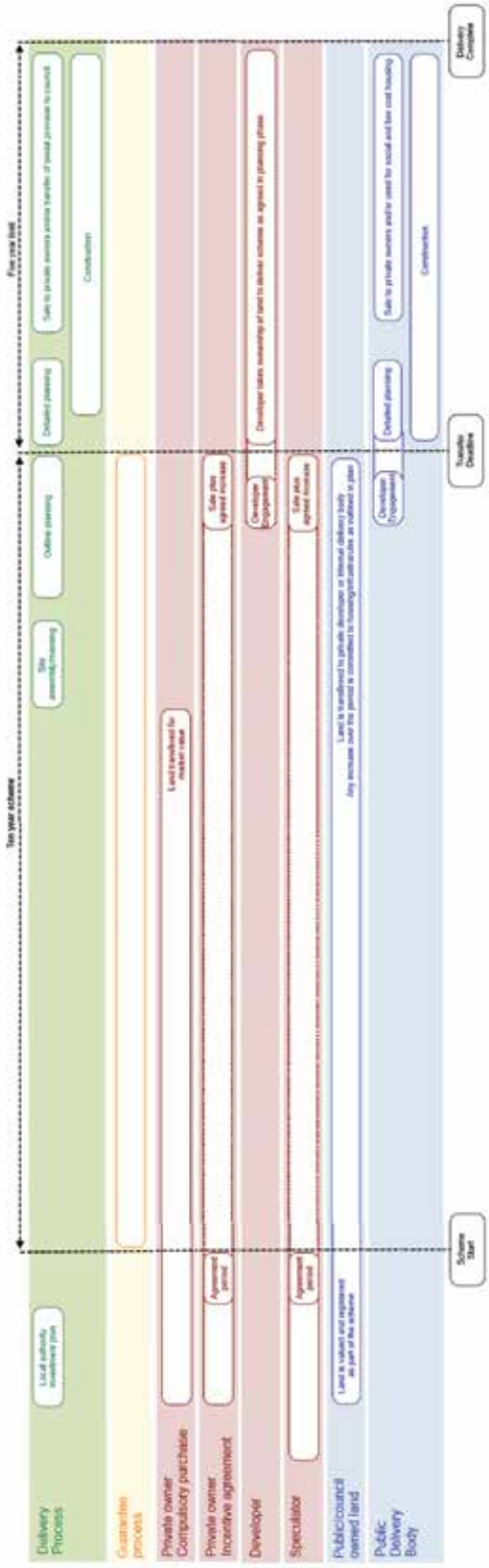
five year period



APPENDIX F

Illustrative schematic

ten year period

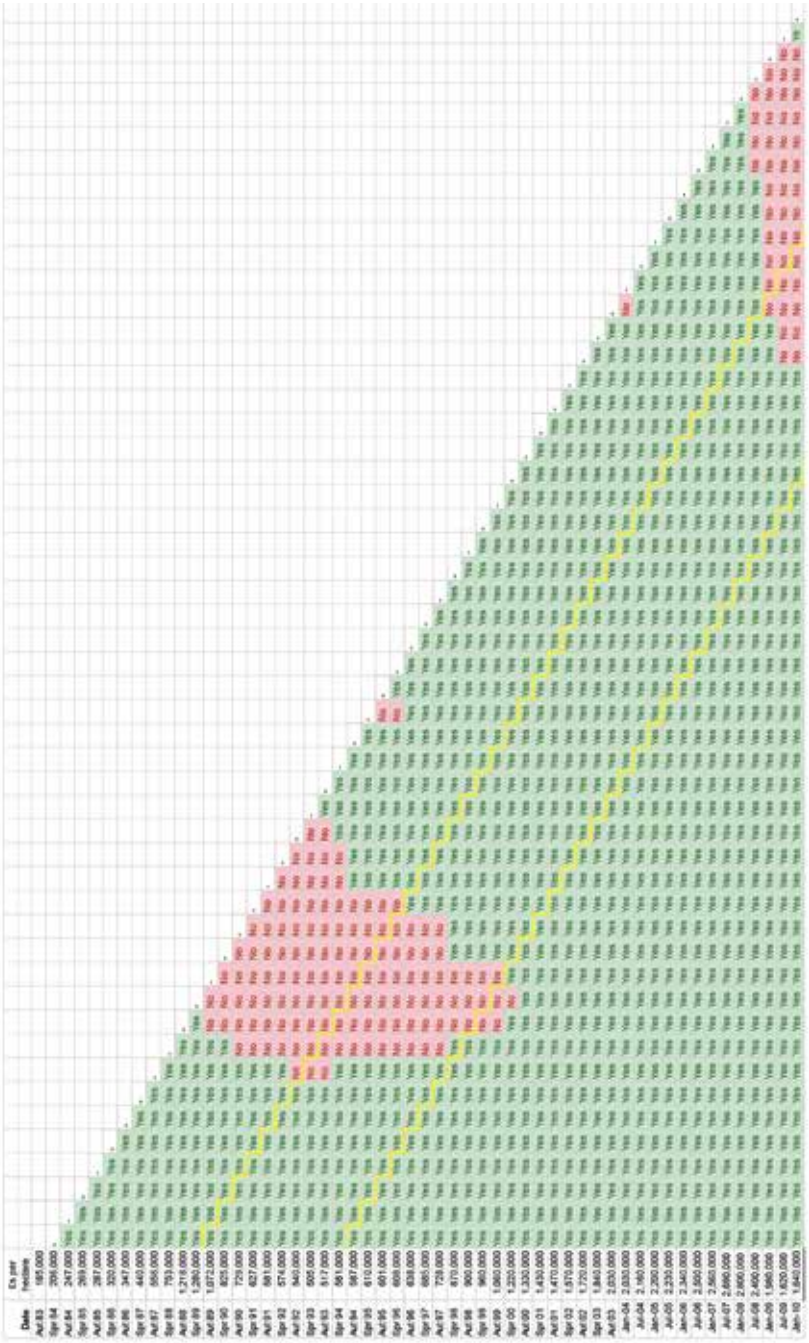


APPENDIX G

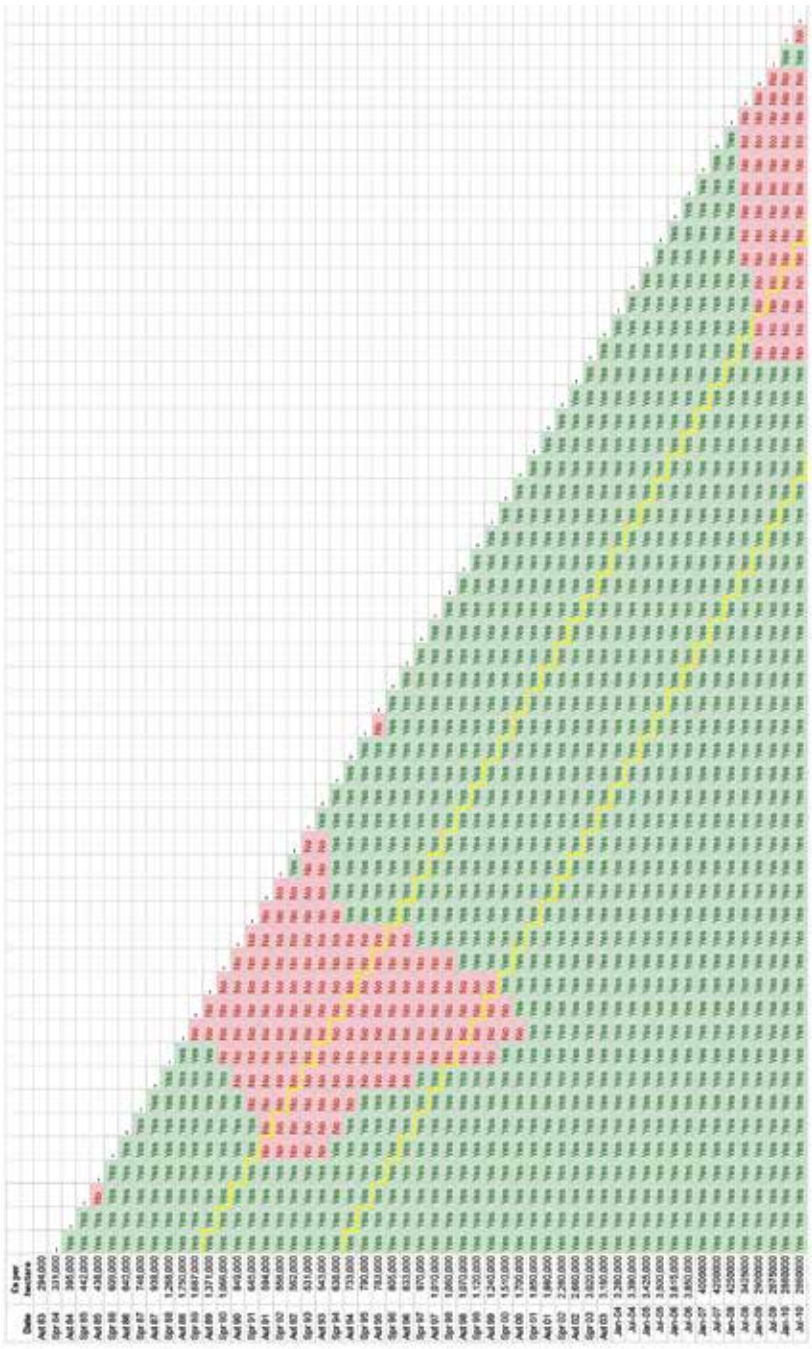
Residential Building Land Figures

Risk distribution entire dataset, with 5 and 10 year fixed periods shown

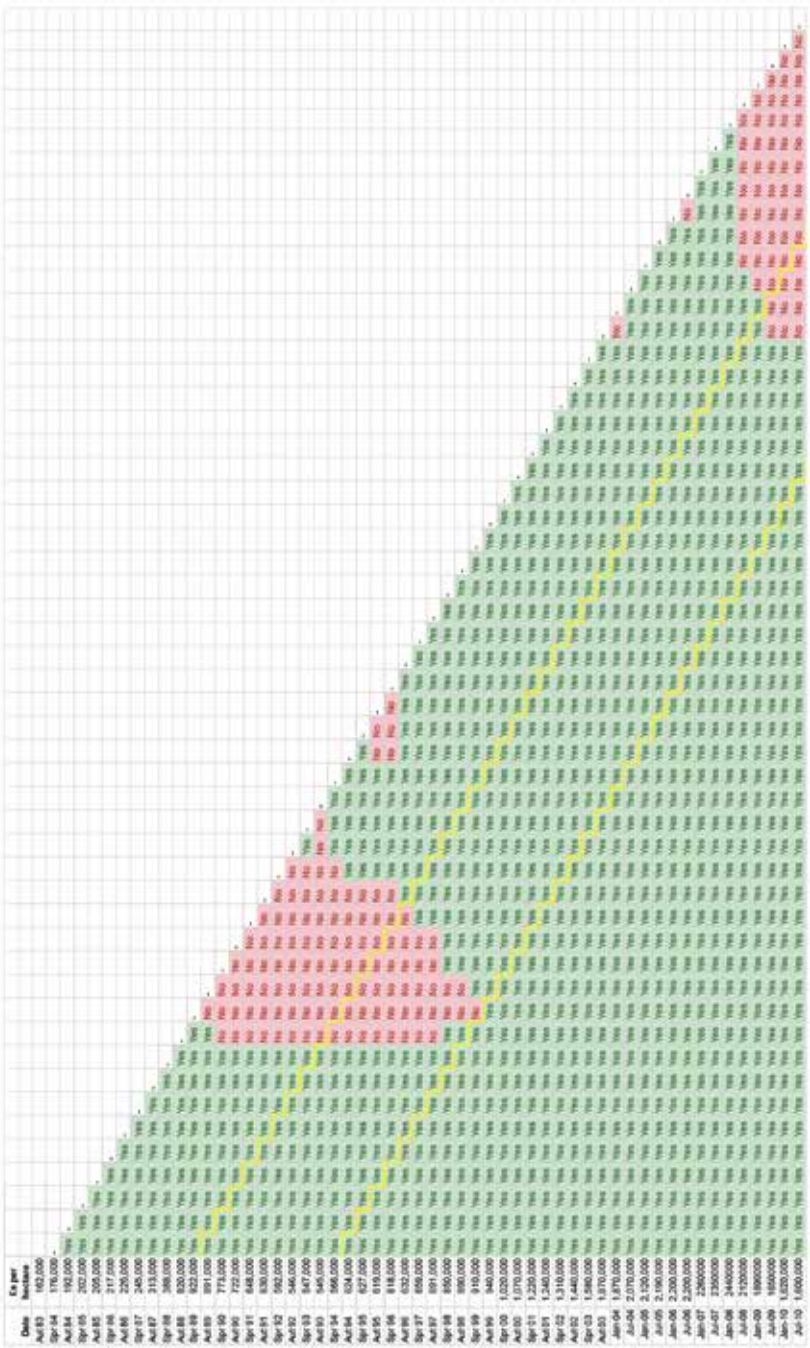
South West



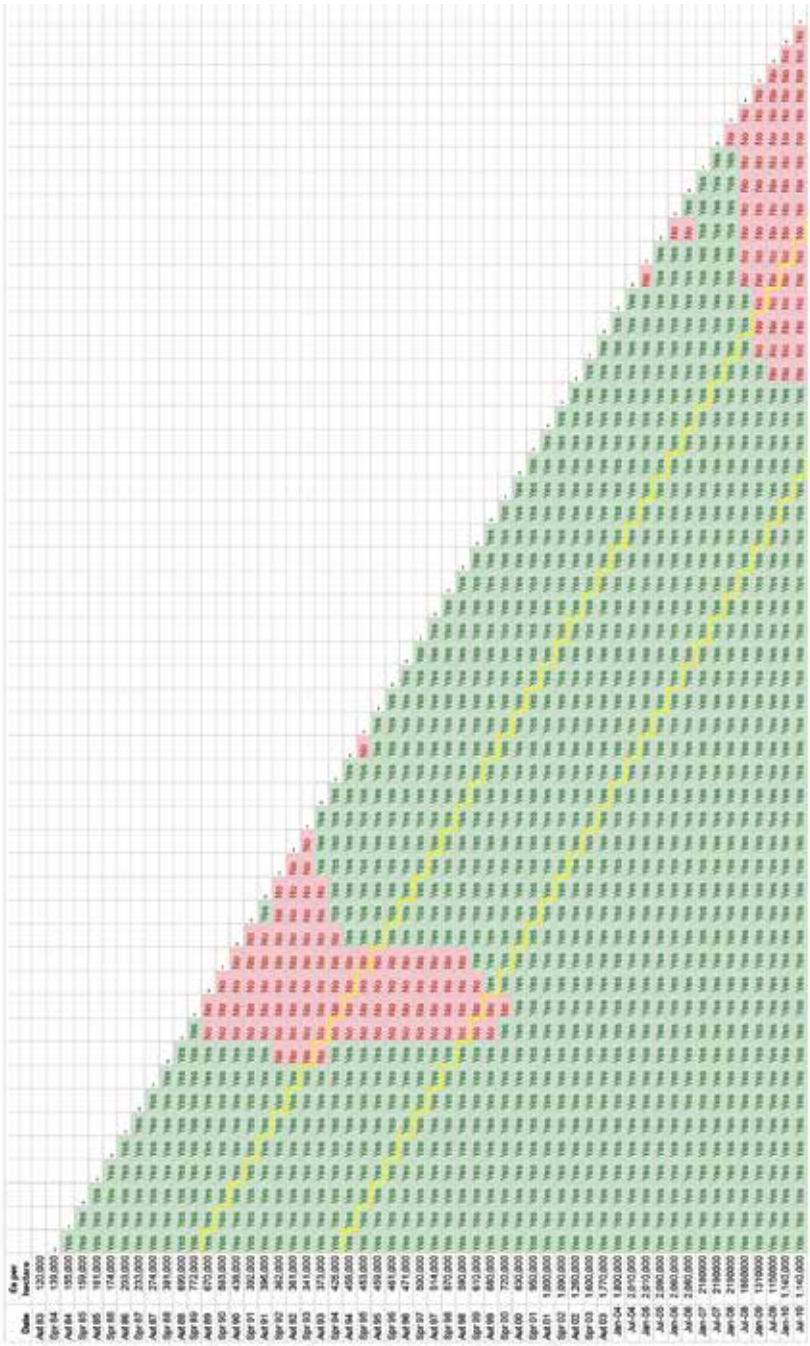
Eastern



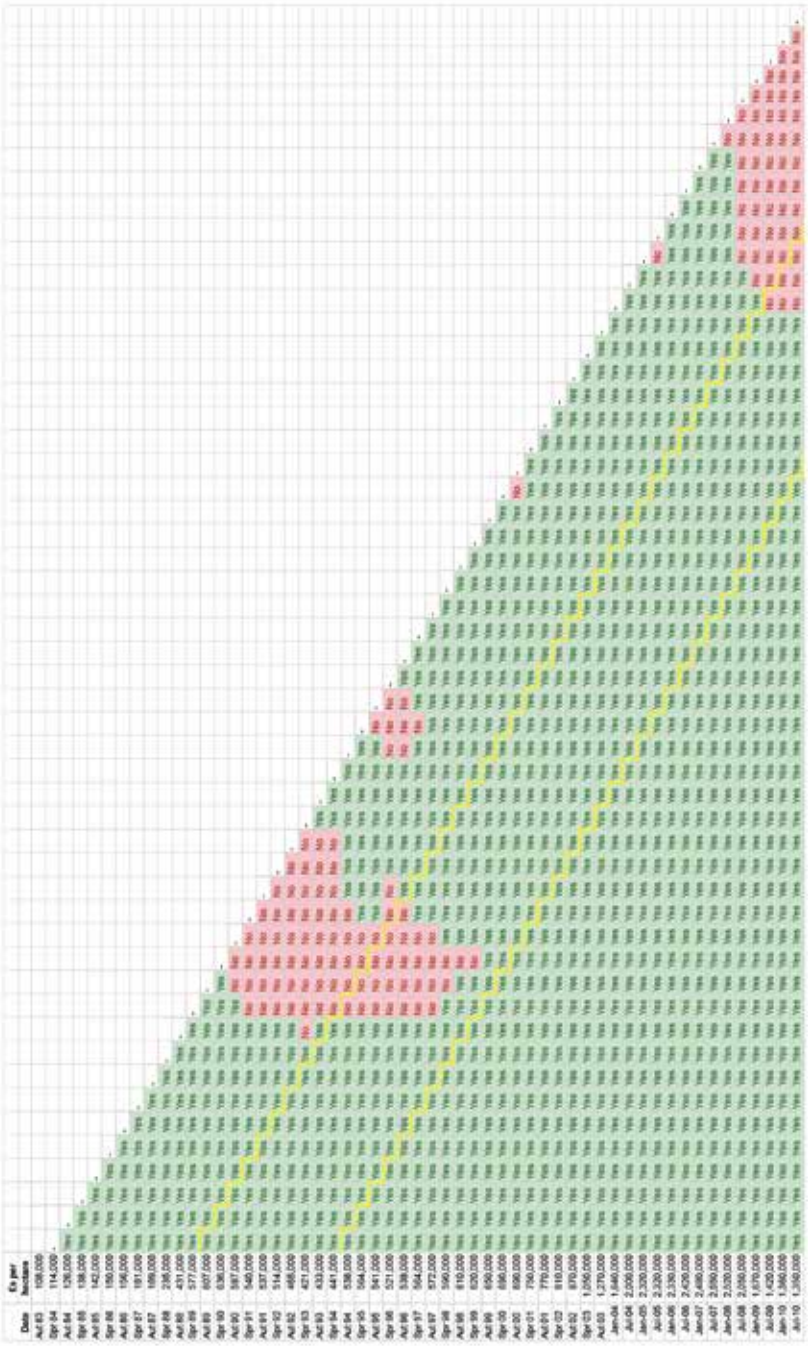
West Midlands



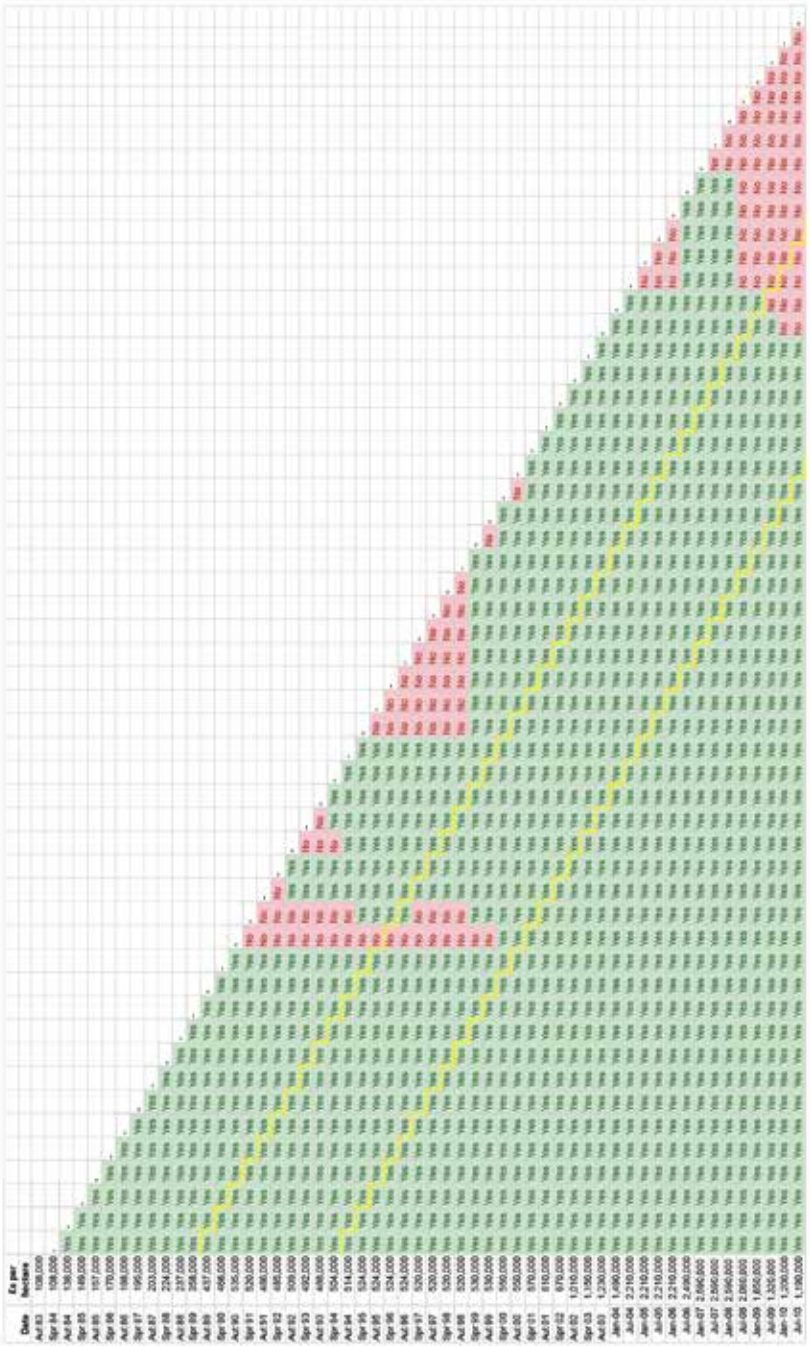
East Midlands



Yorkshire and Humberside



North East



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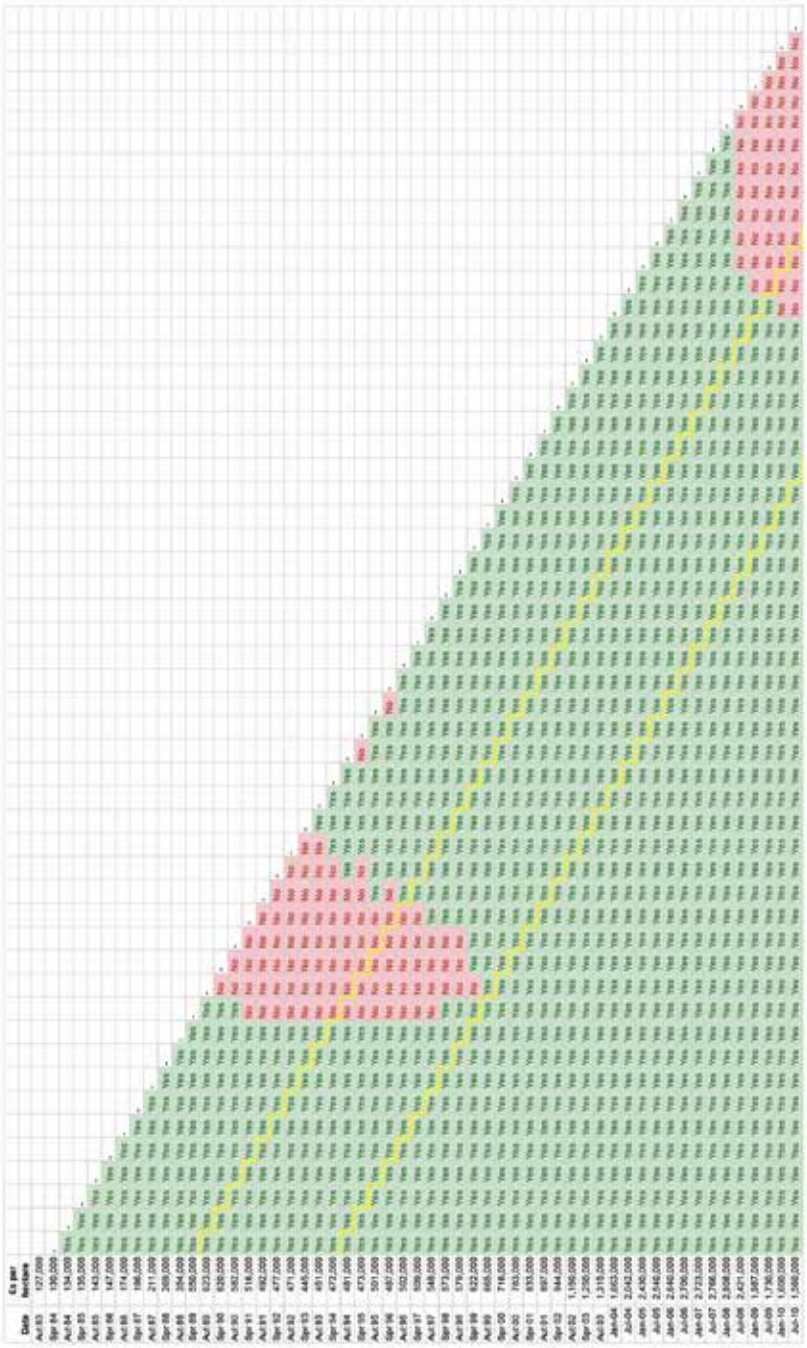

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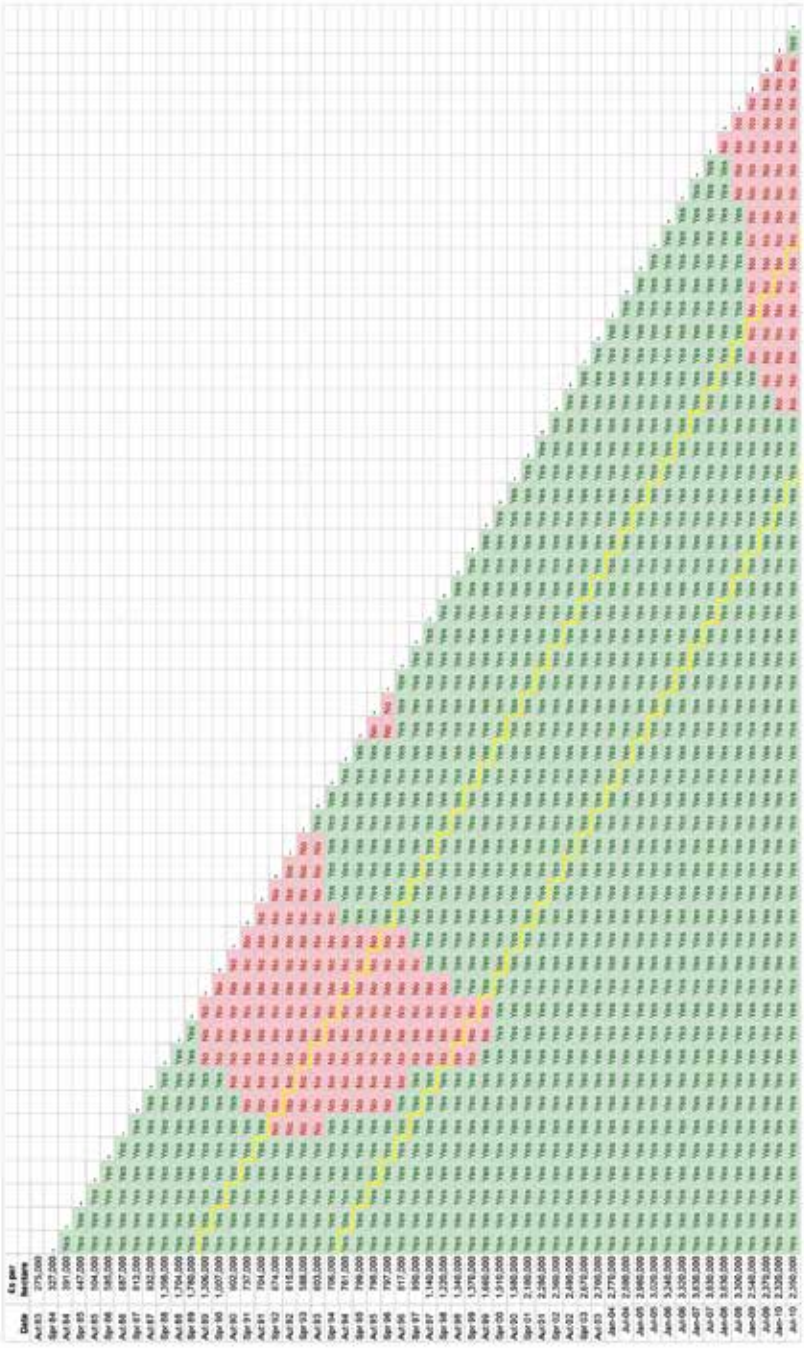
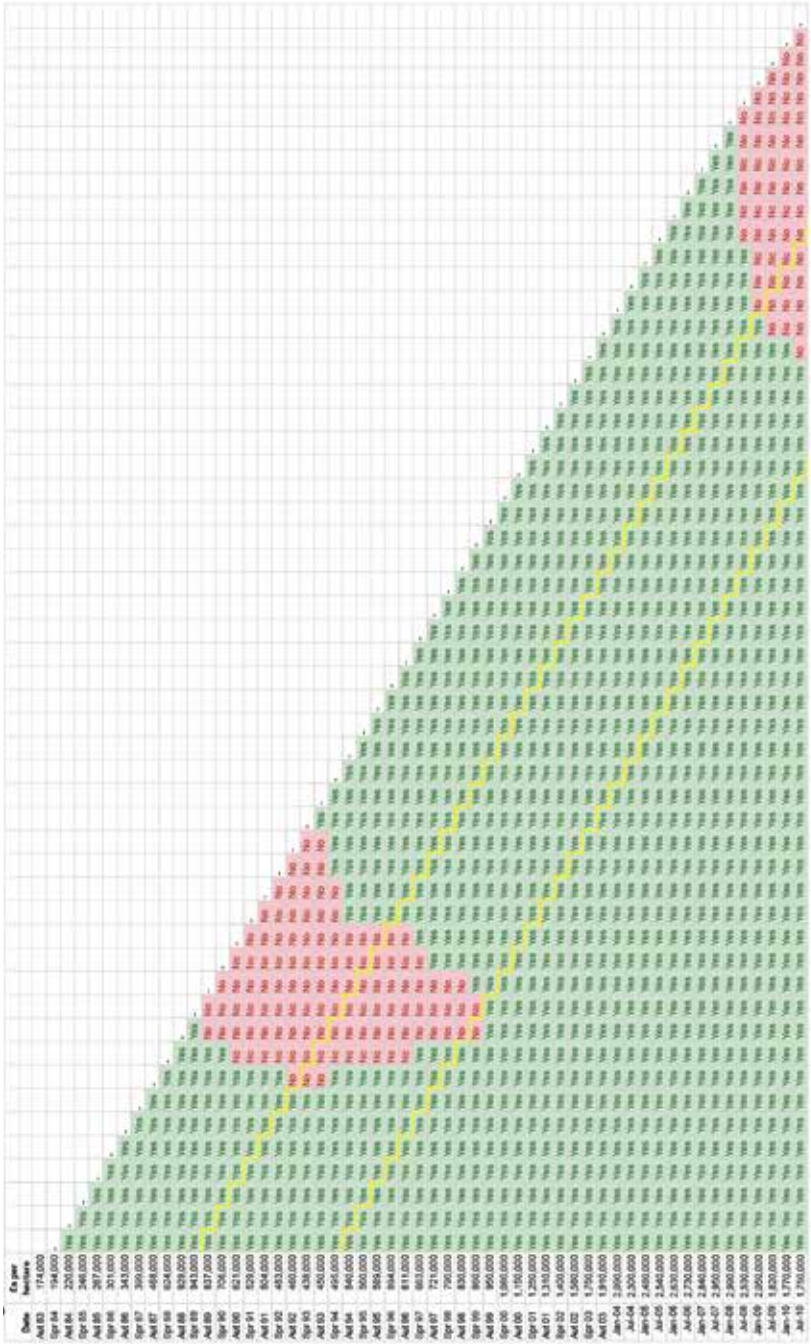
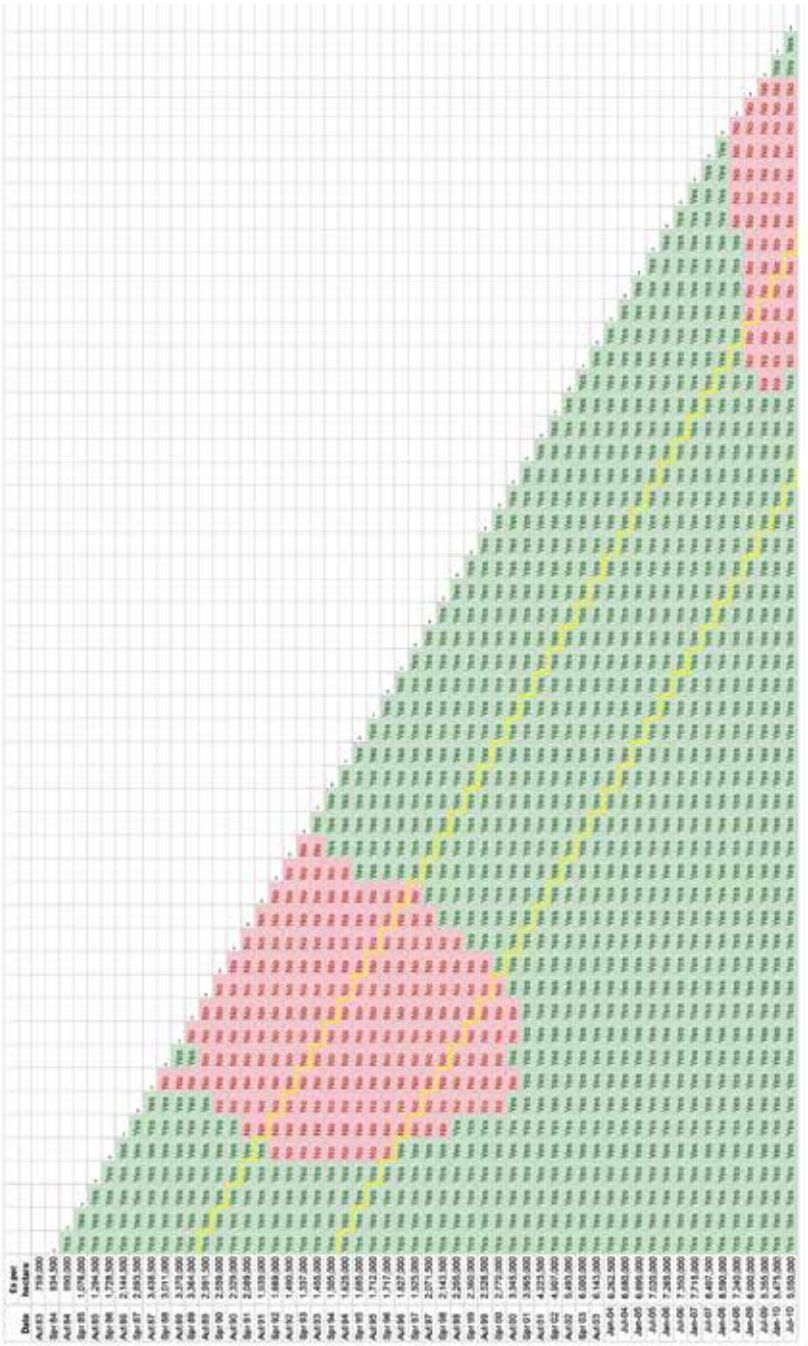


England



London



Endnotes

1 Average calculated using regions/areas in report, therefore provides an approximation of UK average. For full data please contact the Valuation Office Agency

2 Mixed measure used

3 Mixed measure used

4 Property market report 2011, data is possession as at 1 January 2011

5 The land price data is survey based and so hypothetical prices are attached to a 'typical' site for the area in question, with planning consent for residential development and serviced to the site boundary

6 The FTSE index only goes back to 1984. Daily data was used for close for beginning of Feb, July to create a bi annual series. This was then analysed in the same way as the land value data.

7 Latest available land value data

8 Based on the Bi annual data assuming 1 hectares was developed period, which equates to two projects annually

9 CLG, The Incidence, Value and Delivery of Planning Obligations in England in 2007-08 – final report, March 2010 (click here)

10 Parliament.uk, Housing, 17 March 2011 (click here)

11 BBC, House price 'bubble' warning from Building Societies, 18 June 2013 (click here)

12 DCLG, National Planning Policy Framework, March 2012 (click here)

13 Whilst these agreements would be legally binding they would need to consider extenuating circumstances. For example, repeated natural disasters such as flooding may change the viability of a site over a ten year period. Such contractual practices and provisions are already made in industries such as the insurance sector.

14 Whilst this would need further exploration, the guarantee may be index linked to account for inflation over the five year period

15 De Montfort University, Review of European Planning Systems, December 2009 (click here)

16 Kensington and Chelsea council, Planning Obligations, 2010 (click here)

17 Defined on the governments planning portal as in England being the district and metropolitan district councils, London borough councils, unitary authorities, national park authorities, The Broads Authority and the Mayor of London. In Wales, the county and county borough councils and the national park authorities will have the power to charge the levy.

18 De Montfort University, Review of European Planning Systems, December 2009 (click here)

19 CLG, The Incidence, Value and Delivery of Planning Obligations in England in 2007-08 – final report, March 2010 (click here)

ACE economic and policy papers

This paper forms part of a growing portfolio of research by ACE into the effects of infrastructure on the wider economy.

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ACE represents the business interests of the professional service providers in the built and natural environment in the UK. ACE is the leading business association in the sector, with around 600 firms employing 90,000 staff – large and small, operating across many different disciplines – as its members.

Those members are some of the world's leading consultancy and engineering businesses. Renowned for the quality and excellence of their work, they regularly win awards for engineering innovation and achievement.

ACE's powerful representation and lobbying to government, major clients, the media and other key stakeholders, enables it to promote the critical contribution that engineers and consultants make to the nation's developing infrastructure.

ACE's publications, market intelligence, events and networking, business guidance and personal contact, we provide a cohesive approach and direction for our members and the wider industry. In recognising the dynamics of our industry, we support and encourage our members in all aspects of their business, helping them to optimise performance and embrace opportunity.

Our fundamental purposes are to promote the worth of our industry and to give voice to our members. We do so with passion and vision, support and commitment, integrity and professionalism.

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