Q8 consultation – “8. Is the proposed Infrastructure Levy the best way to secure investment in new infrastructure from developers, how might it impact on levels of development? Are there any other ways (to the proposed Levy) that could raise funds for infrastructure provision in order to provide services and amenities to support land development? Are there lessons that can be learned from the Infrastructure Levy as it operates in England?”

What’s wrong with the proposed infrastructure levy?

Stage 1 of the planning bill has proposed a new infrastructure levy from developers towards infrastructure costs to sit alongside section 75 contributions. This would be a charge on the market value of a development per square metre. There is two major limitations of this approach:

a) The levy is unlikely to bring in sufficient funds to make a sizeable difference to the cost of Scottish Government infrastructure for housing provision. The Scottish Government study which proposed the levy (2017) found that a progressive form of the levy would raise £75m annually, while a flat-rate policy would raise just £39m annually. The same study estimates that the total annual infrastructure investment needed for dwellings is £7.5bn, meaning the infrastructure levy would raise maximum 1% of required infrastructure costs.

b) The levy is a charge once development has taken place and therefore does nothing to change the costs of the development process other than adding an extra end cost on to developers for infrastructure contribution. This is a major limitation of this approach, as the costs of land alone can be between 30-50% of total development costs. By reducing the cost of land assembly (the most unproductive element of the development process), not only can the cost of development be brought down but much bigger sums can be raised to contribute towards infrastructure provision. This requires a more ambitious approach which sees raising funds for infrastructure and reducing the costs of housing development as part of a combined, public-led model of development.

Our proposal

Public authorities should have the legal means to purchase land at existing use value, so that the uplift in land value from planning permission for development of the land is captured for the public good. The effect of this will be to reduce the cost of
land for development considerably, as planning permission can increase the value of land by one-hundred fold or more (Evans, 2008).  

The financial consequence of this public land value capture policy will be increased funding for housing development without any upfront cost, as the public authority could borrow against the future uplift in land value to finance the development of the site.

Plots of land can then either be developed directly by the local authority, or sold to developers at cost price plus infrastructure costs. This approach would be significantly cheaper than what developers would pay for development if there costs involve purchasing land at market value, as the value of land is more than three times the value of dwellings in the UK, with land values increasing disproportionately fast since 1995 from £1.5 trillion to £6.8 trillion in 2016 (ONS, 2017).

This public investment would also create better market conditions, as instead of the private sector competing over control of the land market it would compete over the quality of housebuilding developments, creating a more diversified market for housing supply and tenure type.

Public land value capture could be restricted to simplified development zones, creating priority areas for public-led development based on cheap land purchase and self-financing infrastructure provision.

The public gaining from public investment

Public land value capture is not new. The UK Government’s 1947 Town & Country Planning Act introduced planning permission and with it the provision for public authorities to compulsory purchase land at existing use value. This was later reformed in 1959, so that effectively landowners were compensated not at the current value of the land but on its anticipated worth if planning permission is granted for development (known as ‘hope value’).

Public land value capture simply seeks to return Scotland to a situation where the public gains the increase in value from public investment in the development of the land. As Planning academic Andy Inch (2016) has argued, “planning permission is a public gift, restoring to applicants the right to develop land when it is clear that this is in the public interest. Any increase in land values is also therefore the property of the community.”

Land value capture has been utilised in the past by government in the building of Scotland’s New Towns, which each had a public development corporation to compulsorily purchase the land at existing use value, borrowed from the Treasury to

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While there is no comparable figures for Scotland, the Valuation Office Agency (2015) land value estimates for England provide an indication: the average value of an agricultural site per hectare is £21,000, while the average value for a residential site is £6.9m (£2.1m excluding London).
pay for the infrastructure then sold the land with planning permission to private developers, paying back the debt from the land value uplift (Macfarlane, 2017).

**International examples**

In the Netherlands and Germany, public land value capture policies were introduced after the second world war and remain the norm.

In the Netherlands, the Expropriations Act allows local authorities to purchase land at existing use value. Most of the land is then developed cheaply for social housing, and some of it is sold off to commercial developers at a profit.

One example of this was the development by Amsterdam City Council of Ijburg, a completely new neighbourhood built on an artificial island which houses 45,000 people. The council built the infrastructure and master-planned the site. They tied the private sector into the development early by signing contracts for land purchase before the land was ready for release. Companies signed due to the commitment that the Council had already made to the development, reducing the risk in investment (Scottish Government, 2010).

In Germany, ‘urban development measures’ allows municipalities the right to purchase land at existing use value when an area is specified for residential construction. This legal framework means that the state at a local level has a very active role in land assembly in German housing developments, and is one of the reasons why SME house builders play a much more important role in housebuilding, house completion rates are higher than the UK and housing is significantly more affordable (IPPR, 2016).

HafenCity, in Hamburg, is Europe’s largest inner city urban development zone which began in 1997 and when fully completed will contain 5,500 housing units and employ 40,000 workers. The infrastructure for the project was financed through the municipality borrowing against the uplift in land value, which paid for the building of transport infrastructure and public spaces. Land sales to the private sector – with the uplift captured – allowed the municipality to pay back the loans, and attracted 8.4bn Euros of private investment (Centre for Progressive Capitalism, 2017).

**How the financing would work**
The financing of a public land value capture housing development would work as follows:

1) The public authority purchases the land at existing use value, through borrowing from the soon-to-be established Scottish National Investment Bank or through bonds, which will attract significant investment from capital markets due to the security of the anticipated returns. Either way, the interest on the borrowing costs should be extremely low due to the borrower being a public authority and the project being premised on the major uplift in land value which will be accrued once planning permission is granted, which (as long as permission is granted) makes it an extremely safe investment.

2) The public authority will then use the borrowed money on the infrastructure provision and master-planning for the development. Then it will have three options: the public authority can sell off plots to housebuilders to build the homes, using the income to pay back the lender, build the homes themselves, using the rent returns as an income stream to pay back the lender, or a combination of both.

3) Due to the significant increase in land value uplift that could be derived from this policy, it is possible that the public authority could make a profit on its initial investment, which could then be re-invested in new projects. But this would be a secondary aim. The primary financial aims would be three-fold:

a) Provide a financing mechanism to fund infrastructure provision: Under Section 75, public authorities do currently get negotiated agreements for a financial contribution from developers for infrastructure provision. But this
figure does not nearly reflect the total land value uplift that comes from granting planning permission. The Centre for Progressive Capitalism (2017) has shown that Section 75 contributions in Edinburgh were £32 million in 2015-16, more than ten times less than the total land value uplift of £350 million. The public land value capture approach would significantly increase the available capital to finance infrastructure provision for large-scale housing developments.

b) Reduce the burden of housing costs for low-to-middle income earners: Savings in land purchase will substantially reduce total development costs, meaning there should be significant room for reducing the cost of rent when building public rental housing. As research for the Scottish Land Commission (Macfarlane, 2017) has shown, “between 1995 and 2015 the share of income spent on housing costs in Scotland increased by 50%, from 12% to 18%. This was the second sharpest increase of any UK region outside London. The effect of this on disposable incomes has been equivalent to a 13p increase in the basic rate of income tax”. Significantly increasing the available stock of affordable public housing will reduce housing costs for low-to-middle income earners substantially, and thus improve living standards and reduce inequality.

c) Increase the amount housebuilders spend on construction to improve home building quality: The rest of the savings from reduced land costs can go in to improving the quality of construction, to ensure homes are built with maximum longevity and energy efficiency. ‘PassiveHaus’ models of housebuilding are on average 7% more expensive than present social housebuilding models, but reduce heating bills by 89% due to their energy efficiency (industry sources, 2018). With a public rental financial model, the longer the asset lasts the cheaper it costs, as debt repayments on loans can be designed across the life-time of the asset – it would be possible to charge rents 30% cheaper if paying back a 60-year loan rather than a 30-year one.
Consequently the primary financial aims of this model are the opposite of the speculative volume housebuilding industry, which targets the largest profits possible on the basis of the difference between the cost of land purchase, construction and infrastructure versus the sale value to a home buyer/mortgage provider.

The developer under the speculative model has no long-term stake in the development – once it is sold to home buyers, they move on to the next project. This means that they are incentivised to keep all costs to a minimum and sale value to a maximum. Low-costs means:

- Purchasing land where the locational financial advantage is highest, quite often meaning on the outskirts of cities with little proper infrastructure like green space and amenities.
- Constructing homes as cheaply as possible, which means building with materials that are not energy efficient and are not healthy to live in (Fraser, 2016).

Maximising sale value means:

- ‘Drip-feeding’ new homes on to the market so as not to make so many available as to reduce their sale value (new homes built is half the rate of new residential planning permissions granted in Scotland)
- ‘Land banking’ so that other developers cannot build on the land, with the option of building when land values have risen further.

The speculative model negates quality, affordability and proper investment in infrastructure, whereas the public land value capture model incentivises it.

**How projects would be developed**

The project development of a public land value capture housing development would work as follows:

a) Instead of a simplified development zone being established following a request from a landowner/developer, local authorities in conjunction with the Scottish Government’s infrastructure team establish SDZ’s based on their own planning analysis of where essential areas for public-led housing development are needed and can be accessed, as part of strategic and local development plans and with due public consultation. Once the SDZ is agreed by the local authority, Scottish Government and through effective public consultation, the public authority begins the process of land purchase, with the likelihood being that the ability of public authorities to utilise compulsory purchase powers would bring landowners to the negotiating table to agree a deal at a low price.

b) Once bought and planning permission secured, the public authority then builds the infrastructure provision and master-planning for the project in-
house. This will ensure better planned places rather than just housing in isolation, with access to green space, community integration, sustainability and good public transport links prioritised.

c) The plots are then divided between those for public rental housing development and those to be sold-off to the private and community sectors. For the public rental housebuilding, the only sub-contracting will possibly be a procurement process whereby contracts are given on a SDZ by SDZ basis and with specific contractual requirements for build design and quality. Therefore small and medium sized businesses are likely to be able to bid for and win these procurement contracts as they would be small and with a tight contract requirement focused solely on the actual construction of the homes, de-risking investment. For the plots sold to the private and community sector, discounts will be provided to self-build, co-op and community land trust projects to incentivise developments where the housebuilder also lives in the home, a model which encourages quality and sustainability and is currently much more common in the rest of Europe than the UK. The option of leaseholdings for these sort of developments could also be explored. Private sector building projects will be secure investments as the land value element will have been taken out of the development process, meaning housebuilders would make profit solely on building quality homes rather than property and land speculation. The role of the public-sector in delivering the infrastructure and master-planning means investors can have more certainty about the likely level of demand. Social enterprises and other businesses wishing to buy lets for businesses and amenities in the SDZ will be able to do so at cheaper cost than most current urban lettings, due to public authority selling or leasing plots at cost price. This will make it easier for small and medium sized businesses to establish themselves in SDZ’s.

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