



SCOTTISH LAND COMMISSION  
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# **Options for Land Value Uplift Capture**

## **Advice to Scottish Ministers**

17 May 2019



**Purpose: to provide Ministers with initial advice based on recommendations from the Scottish Land Commission’s options for Land Value Uplift Capture**

Over the past 18 months the Scottish Land Commission (SLC) has been exploring options for land value uplift capture. The published outputs from this work, which are all available on the SLC website, include:

- Jones et al. (2018), **An Assessment of Historic Attempts to Capture Land Value Uplift in the UK**, SLC published research report;
- Tolson and Rintoul (2018), **The Delivery of Public Interest Led Development in Scotland**, SLC Land Lines Discussion Paper; and
- Crook T (2018), **Local Authority Land Acquisition in Germany and the Netherlands: Are There Lessons for Scotland?** SLC Land Lines Discussion Paper; and
- Scottish Futures Trust and Scottish Land Commission (2019), **Infrastructure Funding Report**, SFT and SLC jointly published research paper.

## **1. Summary and Recommendations**

There is a strong public interest justification for pursuing policies that would enable more of the publicly created uplifts in land values created by the planning system to be used to support better place-making. It is imperative that this is done in a way that ensures that an adequate supply of development land continues to be brought forward for development. History has shown that poorly designed solutions tend to provoke conflict and resistance, reduce the availability of land for development and ultimately limit the supply of new homes.

It is also essential that any new mechanism or approach is regarded as fair by all parties and has wide-spread political support. To be regarded as fair any new mechanism will need to ensure that landowners whose land is acquired through compulsory purchase receive equivalent compensation to landowners who sell their land on the open market. Simply introducing new rules to exclude hope value from compensation arrangements without addressing this issue is likely to be regarded as very unfair and could breach the protections provided by the European Convention of Human Rights (ECHR).

As many commentators have highlighted, in some other countries that ascribe to the ECHR (notably Germany) municipalities do have the ability to acquire land at existing use value. However, work by the Scottish Land Commission suggests that their ability to do this rests in deep-seated differences between the Scottish planning system and the Dutch/German systems that mean that market value in these countries is closer to existing use value because hope value is very limited. While it would be possible for Scotland to move in this direction, achieving this would require much more fundamental changes than envisaged as part of the current Planning Bill and is unlikely to be achieved through simple changes to CPO compensation arrangements.



In the shorter term, an important mechanism for achieving financial equivalence between landowners would be to use planning policies and obligations to reduce market value (by ensuring that the costs of providing enabling infrastructure are reflected in the prices paid by developers). Existing Section 75 agreements and the new Infrastructure Levy and Masterplan Consent Areas proposed in the Planning Bill could all be used to help achieve this. To this end it is recommended that Ministers:

1. commission a national review of policy and practice in relation to developer contributions and seek recommendations that would help improve clarity and consistency of application across the country;
2. implement proposals to introduce a new infrastructure levy as set out in the in Planning (Scotland) Bill; and
3. use regulations required by the new provisions for Masterplan Consent Areas (MCAs) to require that MCA masterplans provide detailed information about the cost of infrastructure required to deliver the plan and prohibit piecemeal development.

This approach is likely to be most effective in areas where there is significant value to capture but in many parts of Scotland this is not the case. This suggests a need for a more ambitious approach, in which the public sector shares the risks and rewards of development more equitably with landowners and the development industry.

This kind of approach would be an alternative to more confrontational approaches that tend to see large-scale development as a zero-sum game in which the public interest can be achieved only at the expense of commercial interests. In contrast, a public interest led approach is based on the principle that a more proactive involvement by the public sector should enable additional *value to be created that would not otherwise exist*. By creating a framework for landowners and developers to share in this value (“land value sharing”), it should be possible to harness their rational self-interest in pursuit of the common good. A framework for delivering this approach that is consistent with the existing provisions for MCAs contained within the Planning Bill already exists. If Ministers are minded to pursue this, it is recommended that:

4. Ministers acknowledge the need for the public sector to take a more proactive role in initiating and driving forward major development in Scotland and recognise the need for an increased risk appetite to deliver this; and
5. the Scottish Land Commission convenes a working group to draw up detailed proposals to guide the implementation of Masterplan Consent Areas that that build on existing thinking on “urban partnership zones”, public interest led development and the principles described bullet point three above.

Embedding this approach to development is not something that can be achieved through legislation alone. The existence of regionally appropriate partnerships equipped with the necessary skills and resources to drive forward and deliver strategic priorities will be critical. To this end it is recommended that the Scottish Government:

6. works with planning authorities, the Scottish Futures Trust, the Enterprise Agencies and others to establish an approach for identifying and prioritising Scotland’s key strategic development opportunities and provides the leadership and support required to establish appropriate partnerships to drive delivery.



In the longer term there is a need for a more fundamental rethink of Scotland's speculative and market driven approach to identifying and allocating land for development. It is entirely possible for Scotland to move toward a more plan-led system, which better meets the public interest by providing greater certainty for developers, landowners and communities, but this would require much more fundamental changes than are envisaged within the current Planning Bill. In taking forward the next steps of our work in this area Ministers are invited to note that:

- the Scottish Land Commission intends to work with stakeholders to consider what changes would be required to address the deficiencies created by Scotland's market driven approach to land allocation and move toward a less speculative system.

Finally, to help monitor the effectiveness of any new mechanisms and provide a baseline for future assessment it is recommended that Ministers:

- instruct a regular survey of planning authorities to collate data about the volume and value of contributions secured through S.75 agreements and any new mechanisms introduced through the Planning Bill.

## **2. Concepts and Underlying Principles**

Land value capture is a concept rather than a specific policy objective. The term encompasses a wide range of potential policy mechanisms, all of which are designed to capture a proportion of publicly created uplifts in land value.

Publicly created uplifts in land value arise for three reasons: 1) public investment in infrastructure; 2) the granting of planning permission (or the expectation that permission will be granted and some point in the future); and 3) societal factors (e.g. economic growth) resulting in particular locations becoming more desirable to live in.

Broadly there are three main types of land value capture mechanisms: 1) planning-led mechanisms (including section 75 agreements); 2) fiscal mechanisms (like land value tax); and 3) commercial arrangements (like joint ventures). This paper focuses on planning-led mechanisms but the SLC is also looking at the potential role of land value taxation.

## **3. Lessons from History**

The UK has a long history of experimentation with land value capture (see Jones et al., 2018). Early experiments involved attempts to capture the gains from development through direct taxation but these attempts all proved unsuccessful.

One of the reasons for this was that these early attempts tended to be very ideologically driven; designed explicitly to capture "unearned" increments in land value. This was an unhelpful starting point, which made it difficult to secure political consensus.

In contrast the Scottish Land Commission's work on land value uplift capture is rooted firmly in a desire to find effective ways of utilising publicly created uplifts in land values to help fund the infrastructure needed to support good place making. Framing the policy debate in this way is important, not only because it is more likely to generate consensus,



but also because it facilitates a more rounded discussion about how the barriers to successful place-making can be overcome.

The main reason that early attempts to capture land value uplifts were so short lived however was simply that they did not work very well; provoking inertia and resistance rather than increasing development and generally generating less revenue than expected. One of the main reasons for this was that they tended to rely on ill-conceived and overly complex legislation, which gave rise to damaging unintended side-effects.

One of the most important unintended consequence was that taxing development gains removed incentives for landowners to bring land forward for development. This resulted in landowners delaying bringing land to the market in the (well founded) expectation that the legislation would be repealed by the next government. As no serious attempts were made by the state to address this (for example through large-scale state acquisition of land), the supply of land for development started to dry up.

Another important unintended consequence was the creation of two parallel markets for development land in which those who sold land privately received full development value while those whose land was compulsorily acquired received only existing use value. This was widely regarded as very unfair and led to several high-profile cases of serious hardship, which generated significant public pressure for reform.

In 1959 new legislation was introduced that entitled landowners whose land was compulsorily acquired to receive full market value. This established the principle of financial equivalence (under which landowners whose land is purchased via compulsory purchase should receive equivalent compensation to what they would receive if their land was sold on the open market). This principle has prevailed ever since.

**The key lessons from this experience are that:**

- **any successful initiative to capture publicly created uplifts in land value must maintain an adequate supply of land for development;**
- **any new initiative must be regarded as fair by all parties; and**
- **initiatives are much more likely to be successful if they are designed to support a holistic approach to place-making and are not conceived as ideologically driven revenue raising exercises.**

#### **4. Compensation and the Public Interest**

There has been a significant focus within the ongoing policy debate about land value uplift capture on whether it would be possible and/or desirable to amend compulsory purchase rules to enable public authorities to acquire land for development at less than current market value<sup>1</sup>. The rationale behind such proposals is that this would enable

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<sup>1</sup> Existing use value is the value of land in its current use, excluding the value of any potential uplifts that could arise in the future, perhaps because of a change in use. Value attributable to the expectation of future uplifts in value (for example when land secures planning permission) is described as hope value.



public authorities to use any subsequent uplift in land value to help fund investment in the infrastructure and services necessary to bring land forward for development.

The logic underpinning these proposals is sound and there is a strong public interest justification for pursuing this line of thinking, but caution is required because a poorly designed solution could simply recreate the unfairness of the 1950s. This not only has the potential to reduce incentives for landowners to bring land forward for development (which would have a knock-on effect on the supply of new housing) but could also contravene the European Convention on Human Rights (ECHR).

Compulsory purchase of property is acceptable under the ECHR providing it is in the public interest but legal experts have argued that the greater the discrepancy between the full market value of a piece of land and the price the state is willing to pay, the stronger the public interest case must be. Proving that the public interest is strong enough to justify compulsory acquisition at less than market value in any given case would require relying on an untested legal principle, which would be likely to result in lengthy legal cases with no predictable outcome. Even if successful such an approach could very well defeat the objective of speeding up the delivery of new homes.

Part of the solution to this difficulty could be to implement policies that would help to reduce the gap between existing use value and full market value across the board. Rather than seeking to enable local authorities to acquire land at existing use value this approach would instead seek to ensure that the market value of land accurately reflected the infrastructure and servicing costs required to enable development.

## 5. Using Planning Policies to Shape Land Value

There is good evidence that much could be done to achieve this by using existing and proposed planning mechanisms to shape land values. The logic behind this approach is simple. When deciding what to pay for land, developers use what is known as a residual valuation model, which involves subtracting the total costs of developing a site from the total revenue that the site is expected to generate from the sale of completed homes to give a “residual”. This residual then determines the maximum amount that the developer would be prepared to pay to secure the land.

When performing this calculation developers take account of all the costs they expect to incur in bringing land forward for development, including the cost of any planning obligations taxes or levies. Research evidence looking at the impact of developer contributions in England shows that developers have been very successful in passing the cost of planning obligations back to landowners through lower land prices<sup>2</sup>. In this way, planning policies can be an effective tool for shaping land values.

This approach would involve ensuring development plans are up to date, regularly revised and explicit about what land can and cannot be developed and the value and timing of developer obligations. This would be consistent with the Planning Bill’s aspirations to simplify procedures for adopting and updating plans.

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<sup>2</sup> Rowley S. & Crook T. (2016), *The Incidence and Value of Planning Obligations*, in *Planning Gain: Providing Infrastructure and Affordable Housing*, Wiley Blackwell.



### ***S75 Agreements: Making Better Use of Existing Mechanisms***

Although ostensibly designed to mitigate the impact of proposed development, developer contributions have proved very effective in securing the delivery of affordable housing and other forms of enabling infrastructure and as such are rightly regarded as part of the toolbox for capturing land value uplifts.

The longevity of this approach demonstrates that it enjoys broad support but feedback from stakeholders suggests that there are significant variations in how contributions are assessed across the country. This creates uncertainty about the level of contributions that might be expected and when they might be incurred. This uncertainty creates an incentive for developers to pay more for land in the hope that it may subsequently be possible to negotiate a reduced level of contributions with the planning authority.

Providing greater clarity and certainty about the level and timing of developer contributions should result in land changing hands for lower prices, leaving more surplus available to contribute to infrastructure and services. **Ministers could help to achieve this by commissioning a national review of policy and practice in relation to developer contributions to help improve clarity and consistency of application across the country.**

### ***Proposed Infrastructure Levy***

Although developer contributions play an important role in the delivery of local infrastructure, their ability to contribute to the delivery of strategic infrastructure is currently limited. The new Infrastructure Levy proposed within the current Planning Bill has been developed to address this issue.

The Infrastructure Levy seeks to capture contributions to strategic infrastructure through a charge triggered when planning consent is granted that would be applied to most development types. It is intended to operate alongside S75 obligations, reflecting the different circumstances where each can be applied.

The Scottish Land Commission's work with the Scottish Futures Trust involved a financial modelling exercise in which the Infrastructure Levy was compared with a range of alternative funding options, including the Community Infrastructure Levy (CIL) currently in operation in England. The analysis concluded that the proposed Infrastructure Levy was demonstrably more effective than the CIL in its ability to capture uplifts in land value. While the report noted the need for further work on how the Levy might be implemented, the overall conclusion was that it has the potential to make an important contribution to the suite of funding options that currently exist.

### ***Potential Role for Masterplan Consent Areas***

Currently Local Development Plans often require site wide masterplans or development briefs for largescale development sites. These generally show the intended location of onsite infrastructure, how road and transport connections will be made, and the phasing of development but generally do not provide information on costs.

The Planning Bill provides for regulations to be introduced setting out the detail of the MCA process. These regulations could be used to stipulate the information that would be



required in an MCA masterplan and could be used to require a greater level of detail on costs. If this information were to be provided then existing rules on CPO compensation would require such costs to be taken into account in the land valuation exercise, which should reduce the value of land within a designated MCA to a level that reflects the cost of providing the infrastructure required to develop the site.

How close this value might be to “existing use value” is likely to depend to some extent on the inherent development value that the site may have prior to designation. For land that would be expected to have inherent development value, it would be possible to stipulate that planning permission would only be granted as part of a wider development, (i.e. inclusion within the MCA). This would imply that individual piecemeal development would not be supported, meaning that any increase in land value would be directly linked to the designation of the land as part of an MCA.

Prohibiting piecemeal development should have the added benefit of encouraging landowners to participate voluntarily in the scheme, which should help to avoid the requirement for CPO in the first place. Similarly, it may also encourage landowners to collaborate with each other and proactively bring forward proposals to the public sector.

### ***Limitations of this Approach***

Using planning policies to capture uplifts in land value is most effective in areas of relatively high market demand, where development value is high and there is scope for large uplifts to occur. However, development values in much of Scotland are not very high so an exclusively market based approach is unlikely to be sufficient. This implies a more proactive approach by the state may be required to achieving Scotland’s place-making ambitions.

Masterplan Consent Areas could be used as a mechanism to facilitate this but the process of developing a detailed and fully costed masterplan described above would likely require skills that no longer reside in most planning departments. While these skills could be procured from the private sector a more efficient approach might be to develop a collaborative framework that would facilitate collaboration between the public and private sector, enabling both to share in the value created.

## **6. A More Ambitious Approach: Land Value Sharing**

In 2018 the Scottish Land Commission published a paper (Tolson and Rintoul, 2018), which made the case for “public interest led development” where public bodies take a lead role in initiating and driving forward major physical development to achieve specific public policy objectives such as housing delivery or regeneration. Typically, public interest led development projects involve a public body acquiring and assembling land for development, delivering any required infrastructure and/or land remediation and then playing an active role in planning and coordinating the subsequent development.

Delivering this approach would require a much more proactive approach to planning than has been typical in Scotland for many years, but it is not a new idea. The model is often used to deliver major urban development in the Netherlands and Germany and was also used in this country after the Second World War.





A public interest led approach involves the state acting as the “patient place investor”, providing the investment and coordination necessary either to make development happen where it would otherwise not, or to ensure that development is of a higher quality than it otherwise might be. The key defining feature of a public interest led approach is therefore the outputs of the development process are in some way better (e.g. higher quality, more diverse, faster) than they would have been if the development had been delivered by the market acting alone.

This approach would not be a replacement for market activity (successful projects generally involve some kind of partnership between the public and private sectors), but it would require public bodies to accept more of the risks associated with major development. In return, public bodies could reasonably also expect to secure a greater share of the returns to development. This approach could therefore be thought of as “land value sharing” rather than “land value capture”.

### ***Skills and Delivery***

Embedding a public interest led approach to development is not something that can be achieved through legislation alone. Leadership will be required (at a national and regional level) to identify Scotland’s key strategic development priorities and establish regionally appropriate partnerships to drive forward and deliver them. The Scottish Land Commission’s ongoing work on vacant and derelict land, which explicitly considers how such sites could be prioritised for investment, could make a helpful contribution to this.

A crucial factor in the successful delivery of this approach will be the creation of well-resourced, multi-disciplinary teams to lead delivery. Such teams require skills in a variety of areas including finance, land valuation, development economics, property markets and investment promotion. Such skills are often no longer present in local authority planning departments, but they do exist in the private sector and other public sector bodies. Delivering the ambitious approach to “land value sharing” envisaged by the Scottish Land Commission will require new ways to be found to identify and bring these skills together.

## **7. A Framework for Delivery**

In 2014 the Land Reform Review Group proposed a new framework to support this kind of collaborative approach to development. Then described as “Urban Partnership Zones”<sup>3</sup> the proposals are consistent with the Masterplan Consent Area proposals contained within the current planning bill. The concept is based on the well-established practice of land readjustment or land pooling, which is used in many countries to provide statutory arrangements for landowners to share in the financial benefits of redevelopment in return for sharing some of the risk.

The starting point for this approach would involve planning authorities designating an area for major development and entering a joint venture arrangement with a suitable

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<sup>3</sup> <https://policyscotland.gla.ac.uk/wp-content/uploads/2015/08/ULRBP-6-Urban-Partnership-Zones.pdf>



development partner. At this point existing landowners would be offered the choice of either joining the development partnership or selling out to it.

By enabling existing land (or property) owners to benefit from the proposed redevelopment (either financially or by taking reserved space in the new scheme) it is envisaged that this approach would encourage *voluntary* participation and avoid the requirement for compulsory purchase in most circumstances. However, it is likely that some landowners would be unwilling to either sell their land or enter the partnership, so MCAs would need to be underpinned by compulsory purchase arrangements.

Further work would be required to determine what the appropriate compensation arrangements should be for such schemes. The answer to this question will be complex but should reflect the principle that landowners/developers who wish to secure some of the uplift in value arising from the scheme would be expected to contribute to realising that value (by participating in the Scheme). To achieve this it is likely that compensation arrangements would need to reflect both the additional value created by the scheme (above and beyond what would otherwise be achieved), along with the costs of delivering the infrastructure and services required to deliver it (as specified in the masterplan).

Such an approach would be consistent with the use of CPO powers in the Comprehensive Development Areas of the 1960s and '70s (which were used to deliver New Towns across the UK). Uplifts in land values attributable to “the scheme” in these areas were explicitly excluded from compensation arrangements. As a result, there is a well-established body of case law around this concept, which could provide a useful precedent for MCAs

## **8. The Need for Longer Term Reform**

While land pooling has the potential to stimulate activity in designated areas, it is not a panacea and is unlikely to fully resolve concerns about dysfunction in Scotland’s land markets. In many ways the current debate around land value capture is merely a reflection of more fundamental concerns about the effects of Scotland’s speculative approach to development, in which decisions about whether, when and where land is developed are largely left to the market.

This speculative model is not the norm everywhere. Many commentators have for example pointed to practice in Germany, where public bodies take a much more proactive role in assembling land for development and municipalities can acquire land for development at existing use value. This has led many commentators to question why Scotland could not adopt a similar approach.

The Scottish Land Commission addressed this question in a recent paper (Crook T, 2018), which explained how the “deep seated” differences between the Dutch/German planning systems and the Scottish planning system are central to understanding differences in policy outcomes. In particular the report highlights how spatial planning in Germany/Netherlands is conducted in a very systematic way with a formal hierarchy of plans and large public investments in the implementation of those plans.



This approach tends to emphasise legal certainty over flexibility, which means that land values tend to be determined very early on, giving less scope for hope value to arise. In contrast, the Scottish planning system tend to have a much narrower focus on controlling urban growth and land-use changes and provides a much greater level of flexibility. This means that land values do not tend to crystallise until the point of an application being decided, which creates greater scope for land speculation than would be possible under a more plan-led (but less flexible) system.

It is entirely possible for Scotland to move toward a more plan-led system, but this would require much more fundamental changes than are envisaged within the current planning bill. In taking forward the next steps of our work in this area the Scottish Land Commission intends to work with stakeholders to identify what changes would be required to achieve this and move beyond Scotland's current speculative model of development.

## 9. Amendments to the Planning Bill

The Planning Bill contains an amendment relating to the operation of Masterplan Consent Areas that would enable Ministers to make provision for land value capture by compulsory purchase of land. It is understood that the intention of this amendment is to enable planning authorities to acquire land at prices below that for which it currently changes hands to enable uplifts in value to be used to help fund the infrastructure needed to support development.

While this is recognised as a legitimate aim, as currently drafted the amendment is unlikely to achieve its objective and risks challenge under the ECHR.

The amendment is unlikely to achieve its aim because it proposes that compensation should be calculated using a formula that would see landowners receive the value of their land excluding the value attributable to the scheme for which the land is acquired *plus up to a quarter of the value attributable to the scheme*. Under current compensation rules landowners whose land is acquired via compulsory purchase receive *none* of the value attributable to the scheme. As currently drafted the amendment could therefore result in landowners receiving more compensation than they are currently entitled to.

This issue could be resolved by removing sub-section three of the amendment, but the amendment may still risk breaching the ECHR because it is not clear how it would address the issue of financial equivalency for landowners who have had their land compulsorily purchased and those who are able to sell their land on the open market.