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# Social housing and planning gain: is this an appropriate way of providing affordable housing?

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**Abstract.** The current mechanism for providing affordable housing through the planning system in England is based on negotiation within the framework of Planning Policy Guidance Note 3 and Circular 6/98. In this paper the authors examine three groups of questions. First, on the development of the policy, they look at how the need for affordable housing is assessed, how the policy evolved, and how it is currently operated. Second, on the principles and potential outputs of the policy they look at how the approach fits into the principles of betterment taxation, what the results are likely to be 'on the ground' in terms of price and output of housing, and whether these are consistent with taxation principles. Third, they examine what the evidence is so far on the impact of planning obligations on affordable housing provision. Finally, the authors develop a typology of likely outcomes, particularly regarding who pays for affordable housing.

## 1 Introduction

In the British planning system, local planning authorities (county and district councils and unitary authorities) are responsible for setting out their land-use planning policies in development plans and of then implementing them by, inter alia, deciding on applications from developers and others for permission to develop land. Planning authorities are required to take national policy and regional planning guidance into account when drawing up plans and making development control decisions. National policy is drawn up by central government and issued to local planning authorities in guidance notes. Within England, the guidance is issued by the Department of Transport, Local Government and the Regions (DTLR) in the form of planning policy guidance notes (PPGs).

National land-use planning policy for housing has undergone considerable change in recent years, particularly with respect to its role in helping to meet the need for social rented and other affordable housing through planning-gain policies. This has become increasingly important in the past decade, and the most recent central government guidance to local planning authorities in England places the planning system in a pivotal position. The starting points for formalising this policy were the introduction of the rural exceptions policy in 1989 and Circular 1991/7 in 1991 (DoE, 1991). PPG3, published in 2000, not only stresses existing guidance about the need for local authorities to plan to meet the housing requirements of the whole community but also urges these authorities to give priority to allocating land for housing development that reuses previously developed land, to increase the density of development, and to deliver affordable housing (DETR, 2000a).

The increasing focus on higher densities and on reuse of previously developed land reflects the government's commitment to securing the economic, physical, and social regeneration of inner urban areas and to fostering more environmentally sustainable settlement forms. The Urban Task Force (UTF), set up to advise the government on ways of achieving

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its urban renaissance policies, published a report in 1999 (UTF, 1999), and many of its recommendations were incorporated into the urban white paper (DETR, 2000b).

The focus on affordable housing emphasises existing guidance that provision of affordable housing should be a material consideration when residential planning - permission is agreed. In this context, PPG3 requires local authorities: to define what is affordable; to indicate, on the basis of surveys, how many affordable homes are to be provided; to indicate the amount to be sought from developers on specific sites; and to state the intention to seek such an element. The criteria remain the same as in the circular from the Department of the Environment, Transport and the Regions (DETR) to local authorities (circular 6/98)—that there should be a presumption that affordable housing should be provided and that failure to do so could justify the refusal of planning permission (DETR, 1998a).

In Circular 6/98 the DETR also urged local authorities to use the planning system to create more balanced communities by requiring the provision of affordable housing, including social rented housing, in areas where the existing provision is limited and by fostering more private housing in areas dominated by social rented housing. The PPG3 published in 2000 stresses that when affordable housing is secured it should, except in exceptional circumstances, be provided onsite, thus helping to achieve mixed communities. Most fundamentally, PPG3 makes clear that the use of planning gain to ensure the provision of affordable housing and more socially inclusive developments is central to the government's housing and planning policies into the foreseeable future and that planning decisions themselves can no longer be regarded as separate from the question of how the benefits of these decisions are allocated.<sup>(1)</sup>

Placing the negotiation of affordable housing through the planning system at the core of policy on new provision was a major shift in government policy that was further reflected in the government's green paper on housing (DETR, 2000c). Traditionally, social rented and other affordable housing was provided directly by local authorities (and to some extent by voluntary housing associations) with the cost of provision funded by tenants (through rents) and the government (through subsidies to local authorities and housing associations). Now developers are being asked to provide affordable housing within private housing schemes and hence to use market housing to cross-subsidise affordable housing on the same site. The whole thrust of planning policy for affordable housing therefore represents a shift of (at least some of) the burden of providing affordable homes from taxpayers and tenants towards landowners, developers, and, possibly, purchasers of market housing. However, some of the wider government concerns reflected in the white paper as well as PPG3—notably the emphasis on the reuse of brownfield sites, increasing densities of development, and achieving urban regeneration and renaissance policies—can be expected to reduce the capacity to negotiate affordable housing through the planning-gain mechanism (Crook et al, 2001). These policies have not been without critics, especially in relation to the practical issues of implementation (HC, 1998; 1999) but there has been little more formal independent assessment of the outcomes of policy as it has developed (but see Crook et al, 2001).

In this paper we address a number of issues relating to the principles involved, especially the transfer of the cost burden from tenants and taxpayers to other interests. We also examine aspects of practice, particularly the extent to which government objectives of providing additional affordable housing through the planning system

<sup>(1)</sup>At the time of writing, the government issued a consultation on planning obligations that continues to stress this approach while raising the possibility of alternative methods of delivery, notably through a tariff system (DTLR, 2001).

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can hope to be achieved at the same time and through the same policies as the government's wider housing (social inclusion) and planning (urban renaissance) aims.

The paper consists of four main sections: a clarification of the policy in terms of the estimates of the need for affordable housing, the operation of the planning system in relation to affordable housing, and the objectives of current policy; an assessment of how the approach fits with general planning principles, the extent to which this approach can be regarded as a form of betterment taxation, and the impact of such taxation on output and price; a discussion of the evidence on the impact of planning obligations on the provision of affordable housing; and a concluding section in which we develop a preliminary typology of the range of situations that will affect the way the policy might operate and whether such an approach is likely to be successful.

## **2 Affordable housing and the planning system**

Until the mid-1980s the planning system was concerned mainly with projecting overall requirements for the construction of new dwellings and ensuring that there was sufficient development land to meet these requirements. Through the permissions given, the system was able to affect densities but did not directly affect tenure or affordability. Over the past decade the position of the planning system has changed completely as it has become significantly involved in determining local requirements for affordable housing and in enabling these requirements to be met. This has been achieved mainly through negotiating with developers to obtain contributions towards the overall target for affordable new dwellings. The outcome has usually been social rented housing owned by registered social landlords (RSLs), especially housing associations, although there has also been some shared ownership and low-cost market housing.

To explain how this transformation has come about, in this section of the paper we look at three elements: estimates of the need for additional housing and particularly for affordable housing; the development and context of planning policy about affordable housing; and current policy and the mechanisms for policy implementation.

### **2.1 The estimated requirement for new dwellings and for affordable housing**

There has been much debate recently about household projections and the numbers and locations of new dwellings that are needed (HC, 1998; Bate et al, 2000). The 1992-based projections for England, published in 1995, estimated that 4.4 million additional households would be formed between 1991 and 2016, an increase of approximately 25% over a 25-year period. This figure generated greater concern than previous estimates, in part because it covered a longer period than had traditionally been assessed. The 1996-based projections generated a slightly lower estimate of 3.8 million over a different period (1996–2021; DETR, 1999b). However, further evidence, especially from the 1998 population projections, suggests that the impact of longer lifespans and, particularly, of greater in-migration will be higher levels of household formation than those included in the official forecasts (Holmans, 2001).

From the point of view of planning policy, national household projections are only the first stage in assessing how much land should be allocated. Three further stages are necessary: regional and local estimates of projected households consistent with national figures are required as part of developing plans; the relationship between these figures and the land necessary to meet the needs at the local level must be specified; and the proportion of overall requirements that should be affordable must be estimated. Each of these elements generates controversy in determining requirements at every spatial level (Monk, 1999; Monk and Whitehead, 2000).

The national household projections do not imply a similar increase in new dwelling construction everywhere in England. The increase is proportionately much greater in

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southern than in northern England, especially in London, the outer parts of the South East, and in eastern England (Holmans, 2001; Whitehead et al, 1999) suggesting a much greater 'land take' in these regions. [The implications nationally and for regions led to often intense local controversy over plans to accommodate these projected increases, suggesting that it will be very difficult to meet many of the larger increases in areas of tight planning constraints (Bibby and Shepherd, 1996).]

Partly in response to these pressures, previous and present governments have set out targets (currently 60%) for accommodating new housing development on previously developed or 'brownfield' sites. They also stress that more intensive use should be made of the existing housing stock (including converting nonresidential buildings into dwellings) and setting up a number of advisory groups and studies to help achieve these targets and also thereby to foster an urban renaissance (DETR, 1998b; UTF, 1999). In addition, the current government announced a new approach to resolving the 'numbers' question, moving away from a 'predict and provide' approach towards a 'plan, monitor, and manage' approach (DETR, 1998b). This places greater emphasis upon consortia of local planning authorities working together to resolve disagreements about how best to meet local requirements, with a more transparent approach to agreeing the regional planning guidance on these matters and to testing the evidence of an examination in public prior to the guidance being formally issued by central government (DETR, 1999a).

On the need for affordable housing, the most widely quoted estimate was made by Holmans in 1995 (Holmans, 1995). Using the 1992-based household projections, and estimating the likely overall demand for new housing and the need for social rented housing, Holmans suggested a requirement to build just under 250 000 new dwellings in total each year in England over the next two decades. Within this figure, 90 000 affordable homes would be required to meet newly arising needs and a further 10 000–20 000 new dwellings each year would be needed to deal with the existing backlog of unmet housing needs over the forecast period. In more recent work, Holmans et al (1998) estimated that 2.3 million affordable new homes (115 000 per annum) would be required between 1991 and 2011 if newly arising needs were met in full and the backlog were to be reduced by 75%. These latest estimates suggest they are robust to changes in household projections and point to the need to ensure that overall at least 30% of newly built housing should be affordable (Holmans, 2001).

Within this total there is a greater proportionate need for additional affordable housing out of total requirements in the south compared with the north of England (Bramley, 1998). This variation in regional need is strongly linked to evidence on population change, which shows that 80% of the growth in population in the 1990s was located in the south of England (Holmans et al, 1998; ONS, 1999). It is also linked to recent and growing evidence of a surplus of social housing supply in parts of the northern regions of England (Bramley et al, 2000). The evidence includes research showing that recently constructed housing-association stock on local authority estates has proved difficult to let (Crook et al, 1996), that housing associations have more difficult-to-let stock in northern regions than in southern regions (Pawson and Kearns, 1998), that turnover rates in local authority stock have increased substantially (Pawson, 1998), that rents of private and social rented dwellings have converged in certain locations (Freeman and Whitehead, 1996), and that a greater proportion than before of female-headed, lone-parent households now live in the private rented than in the social rented sector (ONS, 1998). Research evidence also shows that demand is falling across all tenures in certain neighbourhoods, particularly in metropolitan areas (Leather et al, 1998). Taken together, this evidence suggests that there are a number of complex processes at work, including a loosening of housing markets in certain

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regions and a revived private rented sector, enabling those who have conventionally been seen to require social rented housing moving instead to low-cost housing in the private sector to achieve lower housing costs and higher neighbourhood quality (Crook, 1998a; Holmans and Simpson, 1999). Matching evidence on national longer term requirements with that on the operation of local markets is thus of growing importance in determining provision.

Over the past five years, only about half the overall national requirement for affordable housing has been forthcoming. The output of new houses provided by housing associations and local authorities for rent or low-cost homeownership has been about a third of the requirement estimated by Holmans and others. This increases to perhaps half when one takes into account low-cost homes built by private housebuilders under licence where the output is sold to the local authorities' nominees and where future sales are restricted to categories of household defined as being in housing need. The shortfall has been met mainly by increasing the number of households accommodated in the private rented sector with the assistance of housing benefit (HC, 1998; Holmans et al, 2000).

As a result of these behavioural shifts there have been suggestions that not all those requiring affordable homes need to be housed by social housing landlords, because some, especially those whose need is temporary, may be better housed within a supported private rented sector. In research for the DETR Peterson et al (1997) attempted to estimate the need for new affordable social housing to 2006, including only the requirements of those with long-term needs for this form of provision (with other needs being supported in the private rented sector). Very preliminary results suggested that much lower numbers of new affordable homes might be needed, although even at this level there would be a shortfall in supply against the current position at the upper end of the range of estimates. Moreover, the estimates were predicated both on a buoyant private construction sector and on increased sharing among rented households.

The discussion in this section on estimates of demand and need shows that there is no simple generally acceptable way of determining requirements. The evidence is clear-cut that housing for large-scale provision to meet the needs of additional households will be required, particularly in the southern part of the country. The evidence is also generally accepted that a significant proportion of these dwellings must be for those requiring some assistance with their housing costs. Equally, an understanding of the local housing system is fundamental to appropriate provision. How the planning system mediates these general requirements is far less clear.

## **2.2 The development and context of planning policy on affordable housing**

Although town and country planning has long been concerned with housing policy matters (for example, in relation to new town policies and urban renewal), land-use planning was not used directly to meet housing need until the late 1980s and the 1990s. Indeed, there was an implicit separation of housing and planning policy until the late 1980s (Crook, 1998b). The task of planning policy was twofold. The first task was to calculate the overall requirement for new dwellings and to set out these requirements in statutory plans and other policy documents at various spatial scales. The second task was to ensure that planning policy then made provision for adequate land to meet these overall requirements, either by allocating specific sites in development plans or by setting out policies to be used by planning authorities when responding to applications to develop other sites (so called 'windfall sites'). Implementation then proceeded through planning applications by both private and public sector housing agencies and by the exercise of development control functions in response to these applications.

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When exercising these functions, local planning authorities did not identify separate affordable housing requirements in statutory development plans until the 1990s. There is no special use class by tenure or affordability. Thus, except sometimes where land is in public ownership, where the principle of best consideration applies, social landlords must pay land prices that reflect private sector market demand, based on the amount that housebuilders are willing to pay for housing land. Some of the development value that accrued to landowners was recouped (at various times) via betterment levies and capital gains taxation. None of this tax gain was earmarked for housing. Instead, the housing policy and finance system gave social rented housing providers (at least in principle) adequate capital finance to compete in the land market and to ensure that the homes built on them would be affordable.

This separation of functions between land allocation and financing was implicit rather than explicit and was always subject to some strain, not least because of the impact that the planning system has on house and hence land prices, especially in areas of tight planning constraints and other areas where the flow of development land with planning permission has been inadequate. In such circumstances, low-income households were likely to have been the losers. In the private sector, they were either priced out of the market altogether or were faced with buying dwellings on new, poorly located, estates built at high densities and low space standards. In the social sector, higher land prices coupled with budget constraints on capital expenditure restricted output and raised the overall subsidy bill.

It was because of these and related concerns that attempts were made in the early 1980s to find ways of using the planning system to ensure that, where development did take place in areas of tight planning constraints, some of that development was targeted at meeting local needs rather than provided on the open market. Many of these initial attempts were indirect, relying on using planning conditions to restrict new development to high-density and small building types as a means of targeting low-income purchasers, allied to legal agreements negotiated alongside planning consents as means of restricting first and subsequent sales of these dwellings to local (low-income) households (Booth and Crook, 1992; Crook, 1996; Jackson et al, 1995; JRF, 1993). The use of planning powers to achieve these outcomes was not generally endorsed by central government. Where local authorities attempted to set out formal policies about 'local needs' in structure plans they were struck out by the secretary of state. Hence local authorities had to use their discretionary powers to bargain and negotiate with developers to provide affordable housing, without the backing of formal policy.

These negotiations on 'off-plan' sites began to be used on a more regular, although still very limited, basis in the latter part of the 1980s in two circumstances: the so-called 'rural exceptions sites' where planning authorities would exceptionally grant permission for housing, provided it met local needs, and, in proposed new settlements, especially in South East England. The use of 'off-plan' sites, however, created significant problems for the status of development plans because it undermined the authority of statutory plans. However, there was strong demand for such policies at the local level, as recognised in a ministerial statement on rural exemptions policies in 1989 and by Circular 1991/7 (DOE, 1991), which set the scene for a consistent formal approach supported by central government.

### **2.3 Current planning policy**

Announcements in 1992 heralded a significant change in planning policy to make it possible for local authorities formally to develop policies related to affordable housing, based upon seeking planning gain. The statement of policy is contained in PPG3

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(DoE, 1992) and in Circular 6/98 (DETR, 1998a). The 2000 PPG3 (DETR, 2000a) developed this approach still further, stating directly that permission may be refused if affordable housing is not provided.

As a result of the changes, local planning authorities may now include policies about affordable housing in their local plans and urban development plans (UDPs). PPG3 and Circular 6/98 make it clear that the need for affordable housing is a material planning consideration that may properly be taken into account in formulating development plan policies and hence in determining planning applications when those policies indicate a case for an element of affordable housing on a site (Grant, 1998). Planning authorities can include statements about the overall requirement for new affordable housing, policies about the measures to be taken to achieve it, including setting overall targets and specifying indicative targets for particular sites, and policies on how to negotiate with planning applicants for these sites, including requiring them to enter into S106 (section 106) planning agreements to secure the affordable housing in the long term<sup>(2)</sup>. Where the total target on allocated sites is less than the overall requirement, UDPs and local plans can include policies enabling local authorities to negotiate contributions on windfall sites. Targets are to act as the basis for negotiations with applicants, not as quotas (DoE, 1992). Advice makes it clear that the definition of affordable housing is a matter for local planning authorities, but that planning policy per se cannot directly address matters of tenure, ownership, or financial arrangements. However, affordable housing may include low-cost market housing as well as subsidised social rented housing.

The 1998 circular emphasised that planning authorities should attempt to ensure that new developments have an appropriate mix of housing and other uses and of different types of dwellings to cater for the full range of housing needs (DETR, 1998a). Indeed, it went so far as to suggest that where there is a large proportion of social housing in an area a significant addition of low-cost market housing in the area should be considered. Where the area consists mainly of market housing a significant addition of affordable housing should be encouraged. However, local authorities have been constrained from attempting to obtain provision on small sites (1 ha outside inner London and 0.5 ha within). Thus, although it is intended to obtain a mix of house types and to “encourage the development of mixed and balanced communities, it is also intended to ensure that affordable housing is only required on sites which are large enough both to provide the implicit subsidy and to accommodate a reasonable mix of types and sizes of housing” and so to assist social inclusion (DETR, 1998a, paragraph 2). The advice also exhorts authorities to pursue affordable housing policies in the wider context of sustainability and the reuse of previously developed sites (DETR, 1998a). It is important to remember that affordable housing may be one of many facilities that local authorities are seeking to capture through planning gain, including transport and leisure infrastructure.

In honouring the obligations, developers originally had several options open to them including:

*option 1:* making provision directly (or in partnership with a housing association) by meeting the agreed proportion for particular sites and thus producing a mix of market and affordable housing on these sites;

*option 2:* making provision on other sites wholly in the ownership of the developers and thus producing the required contribution to the overall affordable housing target, but not by a mix of market and affordable housing on each site;

*option 3:* meeting the obligations by making financial payments to the local planning authority as commuted sums as an alternative to providing affordable housing on the

<sup>(2)</sup>S106 of the Town and Country Planning Act provides for enforceable obligations related to the development and other use of land (see Grant, 1998).



sites in question; these payments would be earmarked for the subsequent provision of affordable housing by other parties.

Under the 2000 PPG3, however, the first option is very much to be preferred (DETR, 2000a), because it ensures that a contribution is made to creating social mix within a defined development site, although the exact relationship between locating affordable with market housing together and the consequent mix of incomes, social classes, and household types will depend on many other factors. Depending on the proximity of the linked site (option 2) or of the site(s) where commuted sums are spent on affordable housing (option 3), options 2 and 3 may also make contributions to achieving social mix, albeit at a different geographical scale.

The policy makes a contribution to greater social inclusion by creating geographical proximity between social groups that would otherwise be more isolated one from another. This, however, assumes that social groups mix in similar ways. This is a questionable assumption as quite long-standing and more recent evidence shows that, although some groups do live their social lives within places, others do so within networks that are not related to neighbourhood (Kintrea and Atkinson, 1998). Whether or not it is desirable to produce this mix at the level of individual *sites* (rather than, say, at the neighbourhood level) to achieve the desired benefits of more mixed communities is beyond the scope of this paper. It may not matter provided that the mixing does not hinder the achievement of the affordable housing objectives or place an undue burden on market provision.

### **3 Principles and potential outputs**

In order to assess either the chance of success or the effectiveness of a particular mechanism it is necessary to understand the principles on which the policy is based and the way the policy might impact on production, price, and the allocation of benefits.

#### **3.1 How the policy fits principles and policies about planning gain and planning obligations**

Although the affordable housing policies described above have now been widely accepted in practice, there have been objections to the principles of implicit taxation involved (for example, see JRF, 1993). Historically, the provision of affordable housing and the taxation of betterment have been entirely separate processes: the government taxes betterment through a nonhypothecated tax and provides subsidy, paid for by general taxation, to social suppliers to provide affordable housing. These processes have now come to be conflated. The general approach was first developed through the use of S106 agreements to enable the provision of infrastructure and services associated with the development for which planning permission was being sought. In this context it was originally required both that expenditures should have some direct bearing on the development and that whether or not permission were granted should not be affected by the nature and extent of the agreement. As such it could, in principle, be regarded as the proper allocation of the direct costs of the development rather than as a levy on the economic rent generated by the permission.

This interpretation is now widely accepted. As a result it is seen as legitimate to require developers to contribute to the costs (capital and revenue) involved in carrying out development, including offsite infrastructure costs, and to mitigate some of the negative side-effects of development. The gradual acceptance of the capacity to 'tax' planning gain in this way stems in part from a growing 'fuzziness' of the boundaries between what should be funded by the private sector and what should be funded by the public sector (Campbell et al, 2000; Healey et al, 1993).

Much less widely accepted is the use of planning gain to require developers to make contributions to wider community needs. Although developers have made such

contributions (often in the form of commuted payments), this practice is criticised on the grounds that there is no direct connection between the development for which permission is sought and the local need for which a planning gain contribution is negotiated. Hence there is no 'rational nexus' (to use US legal language) between the development site and the community need. There is no logical relationship, for instance, between a developer's application for permission to build offices and a contribution sought through planning gain negotiations from the developers towards, say, funds for local community developments.

The extension of the policy to affordable housing through PPG3 in 1992 breached the requirements that the S106 agreement should relate to a direct cost associated with the development, but maintained the principle that the granting of planning permission should, in principle, be unaffected. The 2000 PPG3, however, makes it clear that the number of planning permissions achieved may be modified by the implementation of the affordable housing strategy. Equally, the nature of each planning permission where affordable housing is provided within the development must inherently be modified by its inclusion.

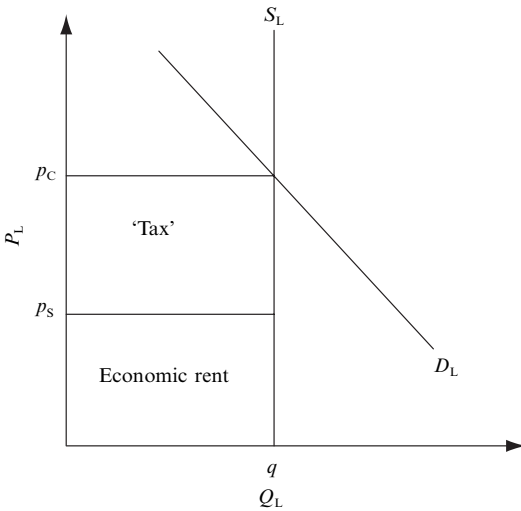
Negotiating with private sector developers to make contributions towards community needs for affordable housing can be seen as a specific case of the taxation of betterment. One argument for such a tax is that, where the supply of housing is restrained in the pursuit of wider planning objectives, house prices and thus housing land prices will be higher; low-income households will suffer and landowners will be the principal beneficiaries (Crook, 1996). There is a logic therefore in attempting to 'tax' some of the income of higher value developments. Attempting to negotiate contributions to affordable housing is one way of taxing this gain—on the assumption that landowners bear (at least some of) the cost in the form of lower prices. Another way is to tax the gain directly (as has been done in the past) and possibly to earmark the tax taken for affordable housing. A third way is the tariff principle, put forward in the recent consultation paper on planning obligations (DTLR, 2001).

### 3.2 The impact of the tax on output and price

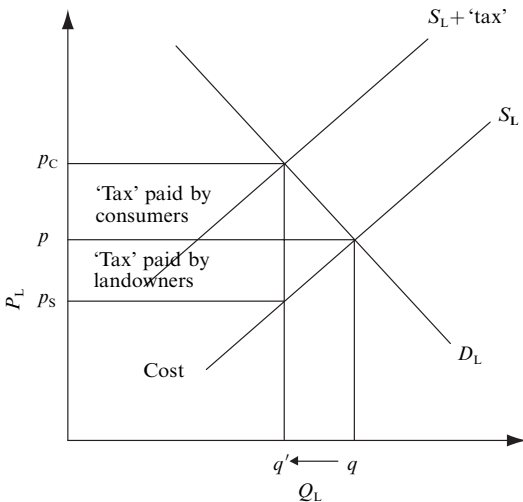
Both the 'taxation' and its hypothecations potentially have important implications for the appropriateness of the permissions actually agreed. By definition these are not the same as would have occurred without the requirement.

In order to assess the arguments for and against any such approach it is important to clarify the underlying relationships between the market and the planning system. Careful distinctions should be made between the impact of policy on direct costs, the supply of housing and land, housing demand, and economic rent (Crook and Whitehead, 2000). Economists usually define betterment as meaning the taxation of economic rent (that is, that payment not necessary to maintain the resources in their correct use). They distinguish this from taxation to ensure the correct allocation of resources (such as those necessary to address differences between private and social costs).

Figure 1 (see over), which shows the relationship between the price of land ( $P_L$ ) and its quantity ( $Q_L$ ), reflects the simplest possible situation where the effect of introducing the 'tax' is simply to fund part of the development. Here the planning system is assumed to be unresponsive to changes in either demand ( $D_L$ ) or cost—so that the supply curve ( $S_L$ ) above the opportunity cost of land is completely fixed (inelastic). The price of land ( $p_C$ ) is demand determined and any tax is paid in full by the landowner: the tax being,  $p_C$  (the price paid by the consumer)  $- p_S$  (the price paid by the supplier  $\times q$  (quantity)). There is no resultant change in the price of land or housing, and the quantity of housing provided remains the same.



**Figure 1.** Affordable housing ‘tax’ paid by the landowner, with no change in output.

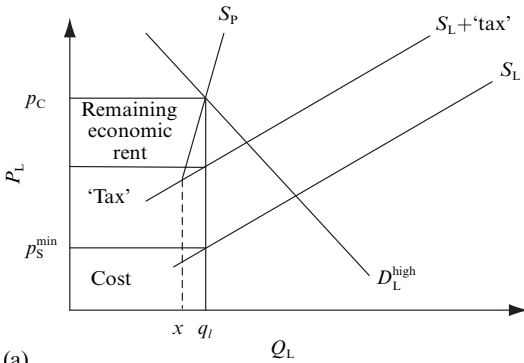


**Figure 2.** Affordable housing ‘tax’ paid partly by the landowner, and partly by consumers, for reduced output.

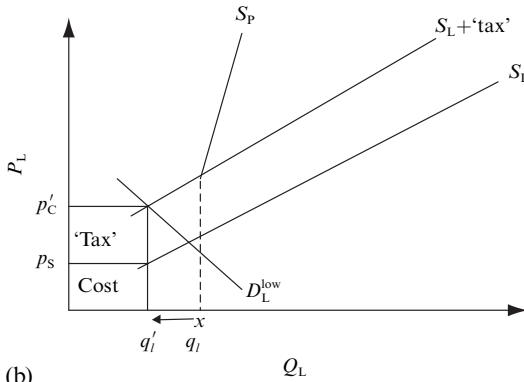
In this context there is no distinction between a pure redistributive tax and one that aims to cover any differences between the private and social costs of provision. Charging developers for affordable housing or for infrastructure would impact on the landowner in exactly the same way as directly taxing the landowner—the price received by the landowner is reduced by the amount of the tax. This is probably the implicit model that policymakers had in their minds when introducing the system of planning gain; that is, it is a ‘win–win’ situation, where output remains unchanged and the gain that specific landowners obtain from obtaining permission is reduced. It is thus strictly a betterment tax. It can tax those who generate external costs but cannot change the extent of those costs.

This version is not consistent with most interpretations of PPG3 and other guidance on housing provision, which make it clear that planning is expected to respond to changes in price (Coopers & Lybrand, 1985; Evans, 1983; Monk et al, 1996). If this is the case the supply curve ( $S_L$ ) is not fixed but is instead upward sloping, with the elasticity depending on the

extent of planning constraint. To help clarify what happens if this were the case, we depict in figure 2 a situation where supply is market determined. Supply responds to increases in price. An affordable housing ‘tax’ is introduced ( $S_L + \text{‘tax’}$ ). The effect is to reduce the supply of land made available from  $q$  to  $q'$ , to increase the price of land from  $p$  to  $p_C$ , and thus to reduce the quantity of housing and to increase both the price and the density of housing provided. Thus landowners and consumers help pay for the provision of affordable housing, and developers pay through reduced output and therefore lower profit (but not in terms of profit per unit, if the construction market is competitive). This type of ‘tax’ is no longer purely a betterment levy. It generates a misallocation of resources unless the ‘tax’ directly reflects the difference between the private and social costs of meeting housing needs and of the particular development.



(a)



(b)

**Figure 3.** Differential impact in (a) high-demand and (b) low-demand areas.

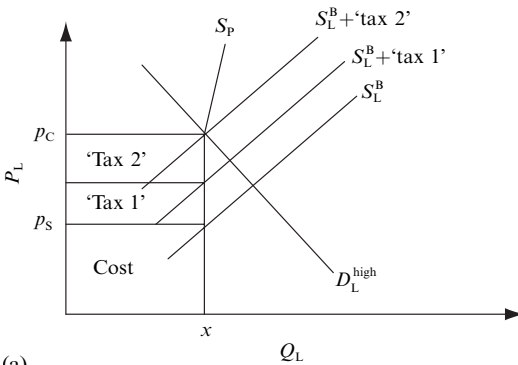
We can build on these two approaches to reflect aspects of current reality (figure 3). The planning system is seen as restricting supply, and that restriction is tighter the higher the demand for land. This is reflected by  $S_p$ . The underlying supply curve shifts upward to the left to reflect the ‘tax’—whether it be one that is based on external costs or whether it be seen as simply redistributive. If demand results in an output above point  $x$ —the point at which planning restrictions start to dominate—the impact of the tax is mainly to redistribute income from landowners to affordable housing. This is more likely to occur in high-demand areas reflected in the demand curve  $D_L^{\text{high}}$ . Owners continue to receive some economic rent and the effect on output and price depends on the responsiveness of the planning constraint to demand. Below point  $x$  the ‘tax’ itself affects market behaviour, reducing output and increasing price. Consumers therefore pay part of the ‘tax’ in higher prices. This is more likely to occur in low-demand areas

reflected in the demand curve  $D_L^{low}$ . In neither case is the tax a pure ‘betterment’ tax. Whether it relates to identified external costs is an empirical matter.

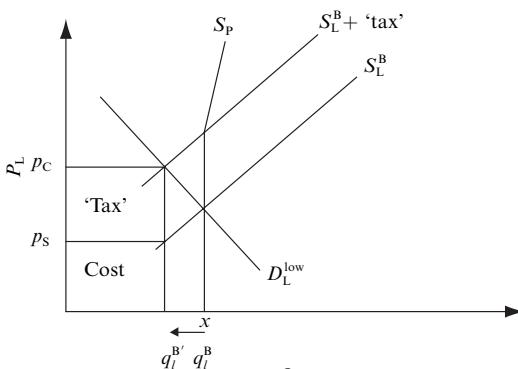
Figure 3 might be taken as a simplified picture of the differences between regions and localities. In the more prosperous areas, mainly in the south of England, where demand is high in relation to land supply, planning gain is easily achieved without significant adverse effects on output and prices. It may also help achieve density objectives. In the lower demand areas, often concentrated in the north of the country, such a tax reduces the incentives to develop and both reduces output and increases problems of affordability in the market. In these circumstances it could be argued that it would be improper to try to obtain affordable housing because it affects the viability of planning permissions.

The likely outcome is further complicated by additional government objectives such as the emphasis on using brownfield sites. It is argued that shifting development to brownfield sites will increase the direct costs of clearance costs and building. The impact is site specific but is likely to have relatively little impact on what can be achieved in higher pressure areas but will further restrict output in areas where there is limited economic rent (figure 4), where  $S_L^B$  reflects the supply of brownfield land. Even in quite prosperous areas it can reduce the potential for achieving affordable housing, turning some locations where there would be surpluses on greenfield sites into ones where on higher cost brownfield sites no such surplus exists. In many parts of the country therefore the impact of government policy on the reuse of land will reduce the potential for achieving affordable housing, and the higher the costs of brownfield sites the greater will be the impact.

There are two important implications for policy if planning permission can be refused in circumstances where affordable housing could be, but is not, achieved. First, those



(a)



(b)

**Figure 4.** Differential impact of brownfield costs in (a) high-demand and (b) low-demand areas.

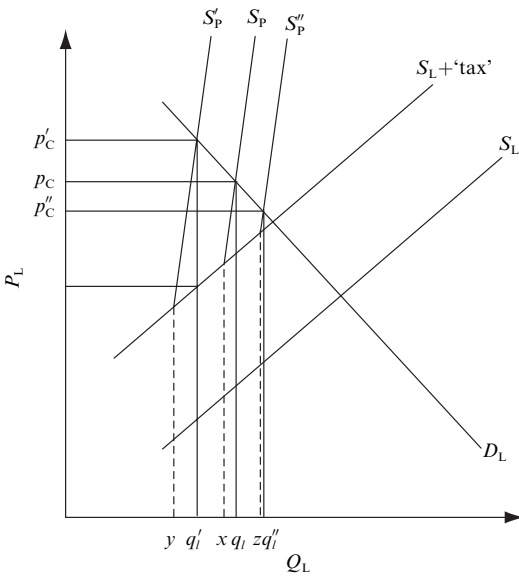
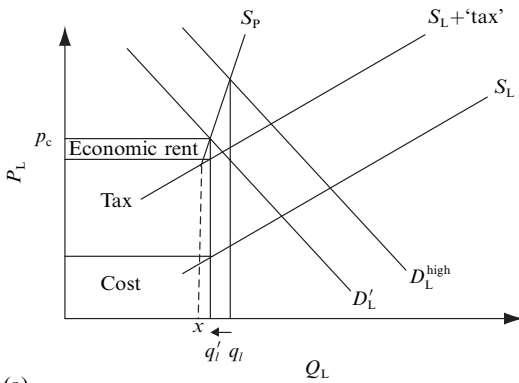
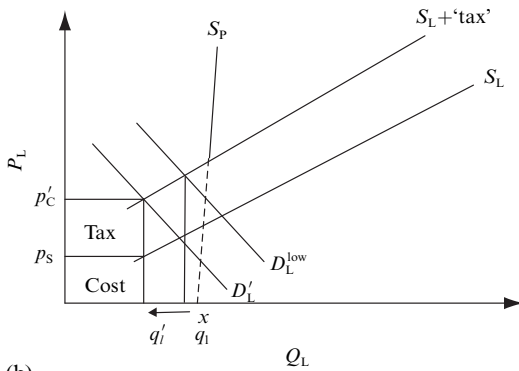


Figure 5. Planning permission endogenous to negotiation.



(a)



(b)

Figure 6. Demand endogenous to negotiations in (a) high-demand and (b) low-demand areas.

making planning decisions must take account of detailed information on costs, prices, and market responsiveness if policy is to be implemented in a way consistent both with reality and the principle that obtaining affordable housing should not make unviable those projects that would otherwise have been able to go ahead. Second, refusing

permission on the ground that affordable housing is not being achieved could shift the 'planned' supply curve further to the left, restricting output and increasing price (figure 5) as  $S_p$  shifts to  $S'_p$  (the more restricted supply curve). There is at least one possibility for offsetting this effect: making a proportion of output affordable may make the granting of permission more politically acceptable, in which the policy could actively increase provision of both market and affordable housing by shifting supply to  $S''_p$  and increasing output to  $q''$  (Holmans et al, 2000). In this case, overall output could be higher and prices could be lower than without the policy.

Last, it is often argued that including affordable housing on site in specific projects may reduce the price of other homes in the area, including those market dwellings included in the project. If this is the case, output will be further reduced as an outcome of reduced demand and prices (figure 6). Again, this limits the capacity to achieve additional affordable housing, although what is provided is itself more affordable. In some circumstances, however, the development might increase the value of the neighbourhood; for example, by reducing dereliction or increasing the overall proportion of market housing in the locality. Here the case for 'taxing' planning gain is stronger because the development has produced a benefit to the immediate community—which should not necessarily simply generate higher income for landowners.

Overall, therefore, there is a wide range of possible impacts of the 'taxation' policy. If the 'tax' simply transfers economic rent there need be no impact on output, costs, and prices. However, in reality, the situation is likely to be far more complex, and the outcomes of such real situations are fundamental to the evaluation of the policy.

### 3.3 Can the policy be interpreted as a betterment levy that is hypothecated for affordable housing?

In order to ascertain whether affordable housing can properly be regarded as a hypothecated betterment levy it is necessary, first, to show that the tax is levied only on planning gain, second, to show that it is generally applied and therefore horizontally equitable, and, third, to show that it does generate additional affordable housing. If these three conditions are not satisfied the approach can be criticised on the grounds that it is improper to require landowners of housing sites to subsidise affordable housing, because this is the responsibility of taxpayers in general. The starting point is to demonstrate that landowners do indeed bear the burden of provision in the form of lower land prices. If this can be shown, critics argue that affordable housing represents an effective site-by-site collection of betterment tax (albeit in the form of lower land prices rather than a specific tax levy).

As the analysis makes clear, whether this is the case depends particularly on showing that the extent of the tax is never greater than the difference between the price of land, excluding the levy, and the private costs borne by the developer. (Even then there is *some* 'nonbetterment' effect if planning decisions respond to demand or impact on that demand.) This in turn depends on showing that market outcomes are not different from those that would have obtained without the policy. That may have been the case in the early stages of the policy. It seems less and less likely to be the case as the policy becomes more central to the granting of planning permission.

In some circumstances the tax is seen as being hybrid—not only to tax betterment but also to bring decisions more closely in line with the underlying resource costs and benefits of decisions. As we have seen above, this can only be the case where the tax modifies decisions (for example, compare figure 2 with figure 1).

The second question is one of coverage and horizontal equity. This requires both that landowners should pay the tax only if it comes from betterment and that all landowners in similar situations should pay. But the affordable housing levy is a negotiated tax—which clearly falls differentially as a result both of legal constraints

on what can be achieved (such as the exclusion of small sites) and of differential negotiating skills across and within planning authorities. It is difficult to see how this can be an equitable tax either on landowners or on others who receive gains from planning permission arising from planning restrictions.

Last, it is unclear whether the affordable housing produced under any of the options is additional to or a replacement for affordable housing that would otherwise have been provided anyway. This depends on whether net additional resources are forthcoming and on whether these resources are used for additional output or, for example, to reduce rents or perhaps increase costs.

Whether the use of S106 produces additional affordable housing (instead of merely modifying their location) depends upon the costs the providers, usually RSLs, face in building the housing (or acquiring them from the developer), the resultant overall grant rate, and the total level of grant made available by government. If the costs are lower (for whatever reason, but, say, as a result of cross-subsidisation by the developer), the system should produce affordable housing that is additional. However, the outcome still depends upon the way the grant giver or bidder treats the lower costs. The impact may be reflected in lower grant rates, in which case the houses are additional as some of the grant can be used elsewhere (or public expenditure saved but at the same levels of output, with the affordable housing scheme displacing a scheme funded at normal grant rates elsewhere). At the other extreme, grants may be retained at the same level as if they were on a 100% affordable housing scheme, saving private debt funding and resulting in rents being lower for that scheme. Although this would not produce additional affordable homes, it would be likely to reduce Housing Benefit payments and/or alleviate employment and poverty traps and thus contribute to the achievement of wider social inclusion objectives.

Thus the overall effect on the total quantity of affordable housing depends on at least six factors:

1. whether central government maintains the level of social housing grant funding and does not substitute planning gain for direct expenditure;
2. whether the affordable housing allocation modifies the overall costs of production;
3. whether the developer (and, through the developer, the landowner) provides cross-subsidy in some way, for example by land prices below market levels or subsidising building costs as well as through direct payments;
4. whether the grant rate for dwellings directly or indirectly provided through the policy is reduced as a result, enabling further units to be provided elsewhere, or
5. whether grant rates are maintained and rents thus reduced, concentrating benefits on those allocated to the housing actually provided; and
6. whether local government modifies its provision of social housing grant as a result of successful negotiations to achieve affordable housing.

#### **4 Evidence to date**

There is still relatively little evidence about the impact of affordable housing policies, especially the extent to which the output of affordable housing from 'planning-gain' sites is genuinely additional. There is rather more evidence on the operation of planning gain negotiations more generally.

##### **4.1 Evidence on planning agreements in general**

Campbell et al (2000) in a recent review of planning agreements found that the use of such agreements had increased significantly in the past decade. This had occurred in a context of declining local government funds and the privatisation of utilities. As a result they have become a major means of funding not only development infrastructure



but also other facilities and services, including the provision of affordable housing (Campbell et al, 2000). In their analysis Campbell et al assumed that the costs of meeting the obligations are predictable prior to land acquisition and that developers can structure land purchase so that the cost of meeting these obligations reduces development value and hence it is landowners who pay. They also suggested that, because the regional variations in the prices developers charge for completed developments are greater than regional variations in the costs of infrastructure, the regional variations in the cost of funding these requirements through planning obligations as a proportion of final prices is greater than if a betterment levy were charged at the same rate throughout the country. In particular they argue that the result is regressive, as the costs represent a higher proportion of final prices in northern than in southern England.

Ennis (1996) examined the costs and benefits of planning gain negotiations from the developers' perspective, using data on planning agreements gathered in five case-study planning authorities. He found that developers' search for profitable outcomes dominated their approach to planning agreements, not their attitude to the legal and other aspects or legitimacy of the policy. They were willing to accept planning gain as a concept, provided they could negotiate agreements that would yield profitable developments. In order to do so it was important for there to be clarity at an early stage in negotiations so they could take account of likely costs in financial appraisals. The case-study evidence showed that developers were able to negotiate satisfactory outcomes and to ensure that their schemes were able to proceed through their own funding of matters such as infrastructure that local authorities were no longer able to fund.

#### **4.2 Specific evidence on affordable housing**

A large proportion of local planning authorities have included affordable housing requirements in their adopted or deposited UDPs and local plans (Barlow and Chambers, 1992; Barlow et al, 1994; HC, 1998). For example, in a survey in 1999 it was found that 78% had specific affordable housing policies in development plans (Holmans et al, 2000). Those who had not done so have generally made positive decisions that additional affordable housing provision is not required. What local planning authorities aim to achieve varies by region and type of development, with the lowest rates in northern England and in inner urban areas. For example, authorities in East Anglia have set targets of 25% to 30% as the proportion of houses in new developments that is to be affordable. In the North West the proportions range from 15% to 20% (Holmans et al, 2000). In London, the Greater London Authority is looking to achieve an average of 50% (GLA, 2000; 2001).

Although limited estimates have been made of the number of dwellings now produced through negotiations, it is generally agreed that the overall contribution is small. One estimate put the output between 1991 and 1994 at 10 000 to 12 000 dwellings (Barlow et al, 1994). The government's estimates for 1998/99 and 1999/2000 were for around 15 000 dwellings—but there is considerable evidence that this covers a number of years and that not all development is actually completed (Crook et al, 2001). Other estimates suggest that 15 000 per annum is likely to be the maximum achievable amount given current overall levels of output (Holmans et al, 2000).

There is very little evidence to date to show whether these dwellings were additional. What evidence there is suggests that not only have planning authorities varied in their ability to achieve their target proportions of affordable housing but also, in the majority of cases, what has been provided has required the injection of social housing grant, both from local authorities and from the Housing Corporation (Crook et al, 2001).

Other evidence suggests that implementation is not easy. There have been problems with definitions of need, with making robust estimates of requirements, with integrating

planning and housing strategies at the local level, with negotiating contributions on a site-by-site basis, and with mechanisms to protect affordability in perpetuity in ways that also protect housing associations' lenders. There has also been concern that some planned developments do not go ahead because financial viability has been undermined (HC, 1998; 1999). Proportions achieved on brownfield sites are also generally lower (Crook et al, 2001). However, the policy has clearly resulted in larger proportions of the affordable housing that has been achieved being concentrated in areas of housing pressure (Curry and Rowley).

To sum up, as predicted there is evidence that the policy works better in some locations than in others. It seems to be more difficult on 'brownfield' and inner-city sites and in the north more generally. It works better on greenfield sites and the south. This regional variation is desirable in that the need for new affordable housing is greatest in the south. The emphasis on brownfield sites does seem to be in conflict with maximising the amount of affordable housing achieved. Most importantly, the very limited evidence on additionality suggests that the increase in the number of affordable dwellings achieved is far below the government's 15 000 estimate of gross provision.

## **5 Conclusions: an interim assessment**

### **5.1 Will additional affordable housing be achieved?**

In this paper we have identified a number of distinctive attributes that are likely to impact on effective implementation. These can be divided into three main groups:

- (1) local preparedness to implement the policy;
- (2) the economic environment;
- (3) the implementation strategy.

For attribute (1), the government is now requiring that all authorities put in place a policy to achieve affordable housing where need can be identified. How much is achieved depends on the authorities' will, their negotiating skills, and the market.

For attribute (2) the most important factors are:

- (a) the extent of demand in the marketplace;
- (b) the costs of production on different types and locations of sites; and
- (c) the impact of the affordable housing requirement itself on the value of the site.

In areas of low demand and high costs, such as inner urban areas in northern England, the potential to achieve affordable housing is likely to be very limited. In parts of the buoyant south, the potential could be very great indeed, especially on greenfield sites.

Implementation strategies [attribute (3)] raise particular issues about:

- (a) the extent of cross subsidy negotiated;
- (b) the availability of additional grant to enable schemes to go ahead;
- (c) decisions on grant rates; and
- (d) the impact of policy on grant levels, both national and local.

To a significant extent the hypothesis must be that under attribute (1) most local planning authorities, except those that can demonstrate low demand, will put in place affordable housing policies but that those where there is little economic rent available will not press too hard to achieve high percentages. Equally, in these areas, what is achieved is likely to require significant additional subsidy to enable building to take place and rents to be held down. In addition, such areas are unlikely to press for allocations on more expensive and difficult brownfield sites—and may indeed rather choose to get market development on these sites at the expense of achieving affordable housing.

These predictions are mediated by the economic conditions discussed under attribute (2). Pressured greenfield areas have high potential for affordable housing;

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low-demand, high-cost areas have less potential, unless output and price are to be adversely affected. The only offset effect here is the possibility that developments that include affordable housing in depressed areas could increase values in these areas and so make some sites viable that would not otherwise have been so. But this would not normally generate much surplus, and so would be dependent on the availability of appropriate grant allocations.

Finally, under attribute (3), the basic requirement is that some additional resources be made available and that these not be offset by reductions in government subsidy, whether central or local. In addition, the increased resources must not all be offset by higher costs or lower rents. When these requirements are met, additional affordable housing will be achieved.

### 5.2 Who will benefit and who will lose?

An affordable housing 'tax' is neutral with respect to efficiency when it is levied entirely on economic rent *and* does not affect resultant output and price. These conditions are most nearly achieved in prosperous areas of high demand and/or at relatively low-cost sites. These are the circumstances where the government states that affordable housing should be negotiated. The proportion of sites that will meet these criteria is reduced by the increased use of more expensive brownfield sites and by the extent that affordable housing reduces prices of the market housing. Even in these circumstances the 'tax' is not neutral if the levy changes the overall number of permissions given. The 'tax' is nonneutral in efficiency terms in areas where costs are increased and output reduced—except when that 'tax' properly reflects true social costs. Equally, it should be remembered that it is not possible to adjust for differences in private and social costs where economic rent exists. Thus the 'tax' plays very different roles in the two types of area.

The 'tax' could, in principle, be horizontally equitable if levied at the same rate across landowners and/or at a rate that reflects community costs. However, in practice, because it is a negotiated cost this is entirely unrealistic. It is vertically equitable if it is levied a higher rate the greater the extent of betterment: that is, at a higher proportion in high-demand than in low-cost areas. To some extent this is reflected in the current Housing Investment Programme and other evidence (Curry and Rowley).

In practice, the 'tax' is likely to be both inefficient and inequitable because of (a) the costs of negotiation; (b) lack of information about the extent of economic rent (betterment) available in each case; (c) the extent of uncertainty in determining land prices between landowner and developer; (d) varying negotiation skills of planners; and (e) who actually pays. The growing range of objectives that central government aims to achieve make this position even more complex.

On the evidence so far, these and other problems (notably the lack of grant finance) are limiting the potential for extracting planning gain through affordable housing. The output is further reduced by the desire simultaneously to pursue affordable housing, social balance, and urban regeneration through the mechanisms of planning control.

It can be argued that there must be simpler and better ways of funding the new affordable housing that is required as well as achieving social inclusion and urban renaissance goals. Suggestions for improvements have been of two kinds. First, there are those that rely most on tightening up the planning-gain 'rules'. An example is the evidence of several professional and lobby groups to the House of Commons Select Committee which examined the draft revised PPG3 and argued, for example, that payments of commuted sums, as alternatives to onsite provision of affordable homes, should be avoided, as these are inimical to the creation of mixed communities (CIH, 1999; HC, 1999). This would almost certainly reduce the prospects for achieving more affordable

housing, as the analysis here suggests that development value is reduced by attempts to obtain site-specific tenure and other types of development mix. Second, there is the possibility of moving away from negotiation to a tariff—as is suggested in the government's planning obligations consultation document (DTLR, 2001). This trades off apparent certainty against flexibility in response to local conditions. It also raises important issues about the priority that will be given to affordable housing as compared with other contributions.

The analysis in this paper suggests that these approaches are unlikely to be successful in simultaneously achieving all three objectives that underlie government policy under current arrangements, both for planning gain and for the funding of affordable housing. If all three objectives are to be achieved, grant rates for affordable housing may have to rise to reflect the higher costs of development on inner-area brownfield sites and the lower prices that may be obtained for market housing. A site-specific and de facto betterment tax is likely to be less efficient and equitable in achieving overall objectives than higher levels of grant funded from general taxation. Equity suggests that, in this case, general taxation should include corporate and private taxes on land transactions. However, local hypothecation can bring with it local acceptance of the need for additional affordable housing. The balance of the argument is unclear; the evidence on outcomes is even less easy to evaluate. What is clear is that land allocation and affordable housing finance are likely to become even more entwined in the future.

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