Proposals to improve Land Remediation Relief to stimulate brownfield development

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Executive Summary

One of the key objectives set out in the Housing & Planning Bill is to strengthen policy on development of brownfield land and small sites for housing. The intention is to introduce Brownfield registers with a commitment to secure a planning permission on 90% of those sites by 2020. The intended policy outputs are primarily to make better use of developable land and to rebuild capacity in the small and medium builder market.

This consultation response sets out how the current Land Remediation Relief legislation can be modified to support these policy objectives. The proposals are as follows:

1. To bring the tax relief "above the line" through the introduction of a pre-tax credit for qualifying remediation costs to operate in a similar way to the Research & Development Expenditure Credit (RDEC). Cost to Treasury - Neutral
2. To increase the value of the tax relief from 150% to 175%. This would have the effect of restoring the tax relief to the same level of cash contribution when the tax relief was first introduced when Corporation Tax rates were 30%. Cost to Treasury - £10m per annum
3. For small sites of fewer than 25 units the relief would be further enhanced to 200% provided the development is completed within 24 months of planning permission being granted. This would again send a clear message of intent to deliver on the 90% target and more importantly to ensure the houses get built. Cost to the Treasury - £3m per annum.
4. To reintroduce tax relief for flood prevention measures. This is a hugely topical issue and would send clear messages to the industry that proper flood prevention or mitigation measures should be incorporated into the development of new homes, also encouraging much needed R&D into mitigation technologies. Cost to the Treasury - £3m per annum
5. To bring forward the date used to determine entitlement to Derelict Land Relief from 1998 to 2008.

The above cost forecasts assume all other aspects of the legislation remain constant other than the proposed modification itself.

This document contains proposals to modify Land Remediation Relief developed and supported jointly by the Environmental Industries Commission (EIC) and the Home Builders Federation (HBF) with assistance of The Fiscal Incentives Group. It is directly relevant to Q7 of the current DCLG consultation on planning policy and development, and to the Government's broader thinking on brownfield policy. Both EIC and HBF are engaged with Government on brownfield policy and continue to submit independent advice and views to Government on this topic. However given the strong commonality of view on the need for Land Remediation Relief reform to drive brownfield development, the two organisations with assistance from The Fiscal Incentives Group have produced this joint submission on Land Remediation Relief.

About the Environmental Industries Commission

The EIC represents the businesses which provide the technologies and services that deliver environmental performance across the economy – we are the voice of the green economy. Our membership includes the bulk of the contaminated land remediation sector, including environmental consultancies, consulting engineers, remediation contractors and soil testing laboratories.

About the Home Builders Federation

The HBF represents home builders who construct approximately 80% of new homes in England and Wales. Our members range from the very large home builders producing over 10,000 homes each year to the small local builder producing fewer than 10.

We hold regular meetings with members and have a number of specific groups such as our Major house builders group, our mid to large house builders and a small developers group. We also have a Tax group drawn from the major house builders which employ specialist tax staff.

It is mid to large house builders who have both the skills and financial backing to undertake the sites that require the most difficult remediation and, in consultation with these members we found widespread support for the proposed changes.

About The Fiscal Incentives Group

The Fiscal Incentives Group is a new consultancy that commenced trading in June 2015 with personnel having come from AECOM, Davis Langdon and previously to that Crosher & James. They specialise in tax incentives for housebuilders, developers and property investors with a particular focus on Land Remediation Relief. They advise many of the national housebuilders and have done so for the last 15 years through previous companies.

1. Need for policy measures supporting development on brownfield land and small sites

*[DCLG '*Consultation on proposed changes to national planning policy' *Question 7: Do you consider that it would be beneficial to strengthen policy on development of brownfield land for housing? If not, why not and are there any unintended impacts that we should take into account?]*

The Government's commitment to brownfield development is welcomed as are the specific policy proposals to introduce Brownfield Registers and Permission in Principle in the Housing & Planning Bill. Whilst these proposals will help to improve the visibility and quality of data on brownfield sites and help remove some of the risk and cost of abortive applications due to declined planning decisions there is still a fundamental aspect of housing policy that needs to be addressed. That is how to encourage the development and housebuilding sector to engage in the development of these sites with all their associated risks and costs.

A key policy outcome for the current set of proposals in the Housing & Planning Bill is to give housebuilders and decision makers "the tools and confidence to deliver more homes in appropriate places" with a priority for brownfield development and small sites. Such confidence will only be achieved if all potential development barriers are considered, not just those associated with planning and identification of sites. Some of the key development barriers are summarised below:

1. Unknown ground conditions: expensive site investigations required and risk of further unidentified issues being uncovered once below ground works commence.
2. Expensive abnormal costs: demolition, remediation, removing or working around underground structures; extra foundation and drainage costs due to presence of made ground.
3. Extra cart away costs: many brownfield sites and especially small sites don't have the space to use excavated material on site. This increases cost of taking material to landfill or alternative development sites.
4. Site constraints: site access and working hour constraints and space for on-site accommodation. Both carry logistics risk and often have cost and programme implications.
5. Proximity to other buildings: complex rights of light and daylight issues as well as party wall concerns introduce further risk, costs and programme implications.
6. Service diversions: many brownfield sites have to contend with expensive service diversion works and for some of the utilities this can result in extensive delay.
7. Flood risk concerns: whilst not an exclusive brownfield issue, many settlements and sites suitable for development are blighted by the increasing threat of flood risk.
8. Ecology issues: sites containing existing buildings and overgrown areas carry an increased risk from presence of protected species, typically bats and reptiles. Capture and translocation is seasonal so can present significant delay to a programme if protected species are present.
9. Small sites: small brownfield sites carry a disproportionate amount of risk due to the inability to easily absorb any unforeseen costs. Also, the preliminaries costs (site overheads etc.) tend to be a much higher proportion of total costs than larger sites.

The reality is that housebuilders and developers will default to the least risky option so the easy to develop sites will almost always be prioritised ahead of the more complex sites. The exception is where there is funding or other incentives available to compensate for the additional risk and costs involved.

2. Funding for Brownfield Sites

There are currently two mechanisms available to developers and landowners to get a contribution towards the cost of developing brownfield sites. The first is grant aid and the second is tax relief. Most grant aid is now administered through the Local Enterprise Partnerships (LEPs) who have the discretion to fund projects from their Local Growth Fund subject to State Aid issues being satisfied. Significantly, the State Aid Block Exemption for subsidising the cost of remediation over and above any subsequent increase in land value was renewed in July 2014 meaning LEPs retain the ability to fund remediation projects. However, this is discretionary and the application process itself can be costly and takes time.

The tax relief on the other hand is certain subject to entitlement and eligibility conditions being met. Based on an extrapolation of data from 8 of the top 15 housebuilders in the UK the forecast is that the current annual cost to the Treasury, or benefit to the sector, is less than half of what is was at the peak in 2007 (see table below).

Year	Estimated Qualifying Expenditure	50% Relief	CT Rate	Cost to Treasury
2006	£197,000,000	£98,500,000	30%	£29,550,000
2007	£215,000,000	£107,500,000	28%	£30,100,000
2008	£224,000,000	£112,000,000	28%	£31,360,000
2009	£101,000,000	£50,500,000	28%	£14,140,000
2010	£73,000,000	£36,500,000	28%	£10,220,000
2011	£80,000,000	£40,000,000	26%	£10,400,000
2012	£82,000,000	£41,000,000	24%	£9,840,000
2013	£100,000,000	£50,000,000	23%	£11,500,000
2014	£124,000,000	£62,000,000	21%	£13,020,000
2015			20%	

This is down to a number of factors including:

1. A reduction in the corporation tax rate from 30% to 20% since the inception of the relief in 2001. This has reduced the cash benefit of the relief for housebuilders from 15% of the qualifying cost to 10%.
2. A general reduction in the scope of eligible works in 2009. This included the removal of water and air as causes of contamination meaning flood prevention measures and mineshaft grouting costs are no longer eligible for the relief.
3. The fact that the date used to determine entitlement to Derelict Land Relief has not changed since the relief was introduced in 2009. The requirement for a site to have been derelict since 1998 means only a handful of sites now qualify for this relief.
4. The condition requiring the acquisition of a minimum 7 year interest in land prior to remediation which has inadvertently prevented some developers benefitting from the relief where there are deferred land transfers.

The result is a tax relief that has suffered from a gradual erosion in value since its first introduction in 2001. In the same time awareness has improved considerably so there is great potential to modify the relief to become more targeted and in doing so support the policy objectives to build more homes on brownfield and small sites.

3. Proposed Modifications to the Land Remediation Relief legislation

The Housing & Planning Bill has set an ambitious target to achieve planning consent on 90% of sites recorded on the new Brownfield Registers by 2020 and to rebuild capacity in the small housebuilder sector from the 2,400 registered builders in 2014 back towards the high of 5,700 in 2006. This is a necessary ambition given the desperate shortage of housing delivery but relies on a largely private and risk sensitive housebuilding sector to engage in the process and to then ultimately develop out those houses. **This is certainly not a given so we believe the answer is to strengthen policy around the current Land Remediation Relief legislation to make engagement in the Brownfield initiative more attractive and by doing so ensuring a greater likelihood that the policy objectives in the Housing & Planning Bill will be achieved**.

The proposed policy areas to strengthen are:

1. To introduce a pre-tax credit for qualifying remediation costs to operate in a similar way to the Research & Development Expenditure Credit (RDEC). The intention would be for the credit to have the same value as the Land Remediation tax relief (equal to 10% (net) of qualifying costs) after the deduction of corporation tax. This would allow the current tax relief benefit to be shown as income and therefore increase the likelihood of the benefit featuring in and influencing the decision to invest. RDEC currently allows large companies to claim a pre-tax credit equal to 11% (8.8% net) of the qualifying R&D spend which is then discharged against Corporation tax liabilities.
2. To increase the value of the tax relief from 150% to 175%. This would have the effect of restoring the tax relief to the same level of cash contribution when the tax relief was first introduced when Corporation Tax rates were 30%.

3. To bring forward the date used to determine entitlement to Derelict Land Relief from 1998 to 2008. Sites currently have to be unused from 1998 (a date set in 2009) to qualify for the relief and now very few sites qualify meaning it is not having its desired effect.
4. To reintroduce tax relief for flood prevention measures. This is a hugely topical issue and would send clear messages to the industry that proper flood prevention or mitigation measures should be incorporated into the development of new homes, also encouraging much needed R&D into mitigation technologies.
5. For small sites of fewer than 25 units the relief would be further enhanced to 200% provided the development is completed within 24 months of an implementable planning permission being granted. This would again send a clear message of intent to deliver on the 90% target and more importantly to ensure the houses get built.

An example to demonstrate the potential impact of these measures is shown below by comparing the impact of the current regime and the introduction of proposed measures 1 and 5. The result is that a site that would not be viable with only an 11.67% pre-tax profit would become viable with a 20% pre-tax profit. The overall cost to Treasury is £100,000 but the result would be 15 more homes built on a site that would otherwise lie undeveloped. This represents a subsidy of less than 4% of the cost of developing the site.

Land Remediation Relief - Current			
House sales revenue		£3,000,000	
Land cost	£150,000		
Remediation	£1,000,000		
Development	£1,500,000	£2,650,000	
Profit		£350,000	
add: LR expenditure Credit			
Profit before tax		£350,000	11.67%

Land Remediation Relief - Proposed LREC & 200% LRR			
House sales revenue		£3,000,000	
Land cost	£150,000		
Remediation	£1,000,000		
Development	£1,500,000	£2,650,000	
Profit		£350,000	
add: LR Expenditure Credit		£250,000	
Profit before tax		£600,000	20.00%

4. **Estimated Cost to HM Treasury**

The estimated cost to the Treasury for these measures is as follows:

1. Tax Credit: Cost neutral with the exception of administrative costs.
2. Increase tax relief from 150% to 175%: Based on the estimated cost in 2014 the additional cost to pay for the increase would be £6.5m. However, the intention is to develop more land as a result of these measures so the forecast additional cost is forecast at £10m per annum.
3. Small Site Relief: According to DCLG statistics the average density to year ending April 2014 was 41 units nationally. It is therefore estimated that doubling the relief on remediation of sites of 25 or fewer units would add c.£3m.
4. Flood Prevention Measures: Flood prevention measures were allowable prior to 2009 and accounted for 16% of the total qualifying costs across our housebuilder clients. We would therefore forecast a cost to the Treasury of less than £4m per annum.
5. Derelict Land Date: the prescriptive and restrictive nature of costs qualifying for such sites means the cost impact is forecast to be less than £3m per annum, equivalent to £30m of qualifying expenditure incurred any one year.

The above cost forecasts assume all other aspects of the legislation remain constant other than the proposed modification itself.

5. **Feedback from the Housebuilding Sector**

Following early discussions with HM Treasury HBF posed three questions to housebuilders. The questions and a summary of the responses received were as follows:

1. To what extent does the Land Remediation Relief cash benefit currently feature in the development appraisal for new development sites?

    - Land Remediation Relief, as part of the wider site remediation strategy, is considered by business units at the development appraisal stage however it is typically not reflected in the financial appraisal models. This is partly a function of the business unit itself being judged on before tax profits.
    - LRR not taken into account in site appraisals – adjusted in CT charge each year
    - Our land buyers are aware of the rules for LRR relief and they do take it into account, up to a point when appraising new sites. There are however limits to this, for two reasons: firstly, the LRR credit is “below the tax line” and it is therefore difficult, in terms of accounting entries, to credit it directly against the associated project – we do not currently do this.
    - Secondly, the quantum of the relief is not known until the LRR work is completed and the corporation tax return is submitted to HMRC, which is often many months after the project has completed and the business has moved onto something else.

2. What impact would the introduction of a RDEC type credit for qualifying remediation costs have on your willingness / ability to invest in contaminated and derelict sites?

    - Changing the mechanics of the relief to an RDEC style above the line credit, i.e. reduction in development expenditure, would drive behavioural change. It would encourage and incentivise business units to invest in contaminated and derelict sites as it would reduce above the line development costs. Taken as part of a package of improvements (such as enhanced rates and redefinition of derelict land eligibility) the changes could make some marginal sites viable.

- Currently not looking at sites with high degrees of contamination – RDEC and LRR are considered as part of the site due diligence but we do not specifically recognise the credit in our site appraisals.

3. In terms of priorities, what impact would an increase in the relief from 150% to 175% have on the number of contaminated and derelict land sites developed compared to a change in the date for derelict land from 1998 to 2008? What evidence can be provided to support this?

- This is difficult to answer, owing to lack of data. However logic would suggest that an increase in the rate of relief would have a wider impact in absolute terms as many sites are contaminated but only a handful are derelict. As mentioned above, a package of measures comprising an RDEC style credit, an increase rate of tax relief, and entitlement to Derelict Land Relief would be the best way to encourage investment in contaminated and derelict sites.
- Increase in LRR to 175% would have a far more beneficial effect on our business. DLR does not and has not applied to us in the past.