Spend today, save tomorrow

The case for reforming CPO 'fair value'

Abstract

The system of calculating 'fair value' for property under CPO acquisitions adds costly construction delays because of the incentive it gives owners to delay and object. Offering substantially more at the outset will reduce objections and cut overall costs

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Foreword

Imagine this. You own a house and one day you learn that your local council (or a government department) is "thinking" of widening the road and if so, will need to use a compulsory purchase order (CPO) to buy your home. It's only a thought at this stage.

You then discover — pretty rapidly — that even though it's only an idea, your home is "frozen" or "blighted". You couldn't sell it — who would want to buy a home that might be CPO'd. You also learn pretty quickly that if you are CPO'd, the maximum you would get is current value plus a bit towards removing expenses. You also discover that even if you did sell your home at current value you might not easily find another one that you like at the same price.

So what do you do? You speak to all your neighbours who are also affected, you get up a petition, you lobby the press and your local MP — indeed you do everything you can to get the authorities to withdraw the idea.

And if you fail and the idea becomes a formal reality, you demand a public hearing and continue to lobby — in fact, you and your neighbours try everything to get the Inspector at the enquiry to turn down the proposed scheme. And if the Inspector approves the scheme you and your neighbours appeal and do everything they can to get the proposals overturned. If you fail and the CPO goes ahead, then you and your family will have suffered significant stress and financial cost over a pretty long period.

Now there is an interesting truth when it comes to council or government schemes — of the total project cost the property purchase cost is usually significantly lower than construction costs. And for every year of delay construction costs rise significantly relative to the land cost. It makes sense if the delays caused by objectors to proposals can be substantially cut.

The solution is actually simple. When a property is needed to be CPO'd the price paid by the acquiring authority should be a multiple of market value — e.g. twice. In essence this amounts to buying off objectors — something quite common and normal in the private sector. If you want to buy something from an unwilling seller you have to persuade the owner by paying more than it might be currently worth.

Now if this were the case then you as the homeowner and all your neighbours will not seek to thwart the scheme as everyone will be very happily compensated if it goes ahead. Even if the proposals are merely a thought, your property/home isn't blighted. Why? Because you and your neighbours will not object to the proposals. If you choose to sell before the scheme is approved the purchaser knows that if CPO'd the appropriate compensation will be paid.

Now I've given as an example one's home, but the same principle applies for all types of property, be it agricultural or commercial. By rapidly getting on with the scheme the overall cost will be far closer to the original budget as a result of avoiding delays — a significant result for the public purse.

It is a widely accepted truth that a small amount of money spent preventing illness will save money in the long run by reducing hospital admissions and the need for expensive treatments. Is there a similar story to be told about acquiring property needed for construction projects that will bring long run economic benefits? I think so.

— Jonathan Harris CBE, FRICS

Introduction

Central, national, regional and local governments in the UK often undertake projects to meet their promises to improve the level of services for citizens of this country. For central or national government this might be an enlarged airport, a new railway line, an array of power stations, or even a major event such as the Olympics 2012. Local governments often need to acquire property for affordable housing developments, new schools, leisure centres and road widening. These projects often involve taking control of chunks of property to enable the construction to go ahead.

The spring budget in March 2020 unveiled a renewed push for investment in Britain's roads, railways, broadband, housing and R&D as part of a goal of "levelling" up the North and Midlands with the rest of the UK. Over the next five years the public sector will invest more than half a trillion pounds (£640bn).[i] This comes on top of the estimated £88bn High Speed 2 (HS2) rail line from London to the Midlands and north of England whose construction work is well underway in north London, Birmingham and Buckinghamshire. These projects will entail the use of a large amount of property currently in private hands.

The system that exists to organise the purchase of that property by the government is known as the compulsory purchase system whose history can be traced back to the Inclosure Act of the 18th century in England and was updated as recently as 2017.[ii] This report argues the system has an inherent flaw in the way it calculates the financial compensation. **By failing to offer property owners a sum money that they will accept immediately, the current system leads to long delays that both push up the cost of the construction project, but also leaves the homeowners, businesses or farmers affected in limbo for several years**. This basic failure requires a radical and innovative solution.

1. Current compensation: 'fair value' is not good value

The system of compulsory purchase by government authorities is a very complex legal area. But it can be summed up simply. Compulsory purchase powers are provided to enable acquiring authorities to compulsorily purchase property to carry out a function which is in the public interest. Anyone who has property acquired is generally entitled to compensation**.** This wording is taken from the introduction to the guide to the system by the UK's Ministry of Housing, Communities & Local Government.[iii] Acquiring authorities either require a Compulsory Purchase Order (CPO) through a specific Act of Parliament or in the case of railway works, an Order under the Transport and Works Act 1992.

Compensation following a compulsory acquisition is based on the principle of equivalence. This means that the property owner should be no worse off in financial terms after the acquisition than they were before. Equally they should not be any better off. The law also says the effects of the CPO on the value of property must be ignored when assessing compensation. The value of the property is therefore assessed on the basis of its open market value without any increase or decrease attributable to the scheme of development that underlies the CPO. The forced nature of the purchase has no influence on the valuation, which is deemed to be an open market transaction between willing parties.

Inevitably owners who had no intention of moving before the compulsory purchase will resent being forced to do so and have strong motivations to resist the proposal. Given that the valuation is a technical process, the more effective weapon is to lobby against the proposal itself and use any inquiry process to lodge objections.

Box A: Quick primer on how CPOs operate

CPOs generally involve eight steps that can be grouped into three broad stages:

1. Preparing the compulsory purchase order.
    - Assembling a list of property interests to be acquired
    - Securing relevant authorisations
    - Preparing the CPO case and submitting it to the Secretary of State for confirmation
2. Public inquiry
    - If there are no objections, then go to stage 3
    - If there are objections, a public inquiry is held
    - The inquiry confirms or refuses the CPO
3. Assuming the CPO is confirmed, exercising the CPO to acquire and compensate the affected property owners.

Several changes were made to the CPO regime through the Housing and Planning Act 2016 and the Neighbourhood Planning Act 2017, which the Government anticipated would make "the compulsory purchase process clearer, fairer and faster for all".[iv] This report will look at those in more detail later.

Since 2008, the rules on major national infrastructure projects were streamlined by the Planning Act 2008 in the wake of the public inquiry into Terminal 5 at Heathrow Airport which lasted for 525 days spread over three years and 10 months. It started in May 1995 and ended in February 1999.[v] There were 41 objectors heard at the inquiry including local authorities and many other statutory bodies. The new rules effectively create a "one-stop-shop" that includes the power to seek compulsory acquisition rights when applying for an order granting development consent.[vi]

Box B: A quick primer on the Planning Act 2008

An applicant submits an application for development consent to the Planning Inspectorate. The public will be able to register with the Planning Inspectorate to become an interested party by making a representation. The Planning Inspectorate must hold an examination and prepare a report on the application to the relevant Secretary of State, including a recommendation, within three months of the close of the six-month examination stage. The relevant Secretary of State then has a further three months to make the decision on whether to grant or refuse development consent. The only challenge at that point is by High Court judicial review.

This process is repeated up and down the country every time a new development is proposed. Delays over relatively small compensation packages have a disproportionate impact on overall costs as an inquiry inevitably adds more time to the approval process for any controversial project. In a society based on democratic capitalism, that is inevitable, and no one would want a system where a government authority can deprive people of their property on a whim.

But the way the system is currently constructed gives every incentive to property owners to throw a spanner in the works that causes delays that will deliver them a minimal benefit at best. The property owner's plight is exacerbated by the fact they will find it almost impossible to sell their land for its current market value once there is any news of a project that might require a CPO order — a phenomenon known as planning blight.

Box C: Planning blight

At the moment, when it emerges publicly that a property might be needed for a project but the CPO process had not begun, even the threat of it makes it hard for the owner to sell their property on the open market. This reduction in value by virtue of the threat of a CPO is known as "planning blight".

The law does provide a mechanism that compels the local authority to buy properties on CPO terms. But the property owners need to prove that they have tried selling the property through a reputable estate agent and have been unable to do so other than at a substantially reduced price. Typically, around six months marketing is seen as reasonable. But even after securing a blight notice, it may take months or even years to agree the compensation.

With compensation under our proposal being set at say two- or three-times fair value, purchasers will not mind remaining in the property in the knowledge that if the CPO does go ahead, they will not only not suffer a loss, but may in fact make a profit.

2. Follow the money

At the moment, the rationale for property owners is clear. As one law firm put it, it is rare for an objection, or even multiple objections, to put a stop to a CPO. "So why bother? Given that an objection by a property owner can compel an inquiry, if used wisely it can significantly enhance your position."[vii] There is also always a chance that the inspector might rule in their favour.

Property owners will use the inquiry route if they do not believe they will receive what is — in their eyes, if not the law's — proper compensation. At the heart of their complaint is often the idea that compensation must only put them in the position they would otherwise have been. Why should they not share in any of the extra value that will accrue to the developer if their land is purchased and the project built?

As David Mundy, partner, and parliamentary agent for legal firm BDB Pitmans, put it in May 2019, fair valuation and the related topic of land value in the context of compulsory purchase raise difficult questions. Why, for example, should increases in value arising from planning permission or new infrastructure not be fairly shared between the dispossessed owner whose property is required in the public interest and the state body acquiring the land to invest in the scheme?[viii] The current reason is that the law prevents it happening.

A 2019 inquiry by the Commons Housing, Communities and Local Government (HCLG) select committee said that according to Government statistics published in February 2015, agricultural land that is granted planning permission for residential use would, in England (excluding London) on average, increase in value from £21,000 per hectare to £1.96 million per hectare.[ix] The amounts involved with respect to brownfield sites vary considerably, although the same Government figures estimated the value of a typical pre-permission industrial site to be £482,000 per hectare. The Greater London Authority and Transport for London highlighted a study by real estate advisors, GVA, which found that development dependent on the new Elizabeth line of the London Underground would create a potential value uplift of £13bn in residential values and £215m in commercial values by 2026. Taken at face value the GLA/TfL figures would translate to an uplift of as much as 92-fold per hectare.

The HCLG committee added another concern: that, in many low-value areas, the financial compensation offered by local authorities or central government for property is not sufficient to purchase an equivalent replacement elsewhere. One witness, a barrister, highlighted the example of a derelict former-mining village near Newcastle, where houses were compulsorily purchased by the local authority at such a low value that it was not possible to find a new home to replace that which had been lost. The National Farmers Union highlighted a similar concern, arguing that a farmer may have land compulsorily purchased which then renders the farming business unviable because of decreased land area.

3. Time for radical reform

The Government has taken meaningful steps to tackle some of the problems with the current complex system. The Neighbourhood Planning Act 2017 tackled the issues arising from the

so-called “no-scheme world” assumption. This had built on the idea of “equivalence” by saying that compensation received would not be reduced because the land had been blighted by the project but at the same time the landowner did not receive a bonus because of the higher value caused by a project that relied on a CPO.

As the Law Commission said in a 2002 consultation paper: “After 150 years of evolution, the present law is a complex mixture of statutory and common law rules, with many unresolved conflicts and inconsistencies.”[x] The provisions in the 2017 Act gave the assessment of compensation for land taken by compulsory purchase a statutory footing. They also provided clarity to the no-scheme world that in determining compensation, any increase or decrease in value caused by the scheme of acquisition should be disregarded.

However, it also took the step of extending the definition of the scheme to allow for specific transport infrastructure projects to be disregarded. The reason for this change was to prevent those owners served with a CPO for a regeneration scheme securing increased compensation for their site when that increased land value could be attributed to a transport scheme, such as a new road which opened up that site for redevelopment. This is likely to lead to acquiring authorities looking to limit compensation for such schemes.

None of the tweaks addresses the inherent problem — that by trying to save a few pennies over the property acquisition may mean losing pounds in the overall project bill. We saw earlier that government guidance confirms that it may be “best value” for an authority to pay slightly more than may otherwise be due to a landowner. It is that logical implication — that it will reward the acquiring authority to pay more than “fair” value for land to avoid or shorten an inquiry — that points the way to a more radical solution. Rather than have the “price” of withdrawing an objection set on a case-by-case basis where the persistence, wealth and character of the objector may carry as much weight as the strength of their case, it makes more sense to streamline that system.

The logic is straightforward: any acquiring authority (AA) will usually want to minimise the number of objectors before any inquiry starts. Shorter inquiries are usually cheaper, and the authority and developer may be concerned about the public relations damage from significant objections. If an inquiry can be avoided altogether, that is even better. So, an AA is often most willing to reach agreement with property owners during the crucial window offered by stages 1 and 2 in Box A. In fact, in recognition of these benefits, government guidance even confirms that it may be “best value” for an authority to pay slightly more than may otherwise be due to a landowner, to remove their objection before the inquiry.

The radical solution proposed in this cuts that Gordian knot by making a compensation offer that no rational property owner will refuse. This will vault over the arena of conflict, delay and uncertainty that an inquiry brings. **The “fair” value of the property that the acquiring authority and developer wants to pay is X, then change the law so the compensation is a multiple of that, whether twice, three times or more.** While it might look to be a crude calculation it solves two problems:

- The authority can reduce the knock-on costs of a long inquiry

- The property owner will know they are being appropriately compensated for being forced to sell.

In essence this amounts to buying off objectors — something quite common and normal in the private sector. If you want to buy something from an unwilling seller you must persuade the owner by paying more than it might be currently worth.

Critics of this proposal will counter that this is "over-compensating" losers from major construction projects that history shows may not always deliver the benefits offered at the time of their proposal. That argument has some weight but is more of a criticism of the failure of adequate forecasting by government department than a valid criticism of the proposal in this report. This so-called "optimism bias" may mean that projects such as HS2 do not pay for themselves, but if the project is going ahead anyway then the idea of cost-effective compensation still holds.

Of course, there will be people who will say that the British government could never adopt such a rationale. They say that time and again, Whitehall would rather pay the long term costs of societal problems rather than investing upfront to solve them — the health costs for treating obesity, and the expenditure needed to detain people with mental health conditions in hospital are just two examples. This is partly due to the government's ability to assess cost rather than value. This is compounded by the fact that the agency which needs to make the initial investment such as HM Treasury is not the same as the one that will reap the rewards. This is connected to the short political life cycle of governments which means the administration that invests now may not be the one that receives the gains in five years' time.

But these arguments are not convincing — they are ways of saying that because an eminently sensible policy has not been pursued in the past it should never be adopted. That is plainly nonsense: achievements such as the legalisation of abortion in Ireland and the introduction of a national minimum wage in Britain would never have happened without a willingness to change.

Clearly the reform proposed in this report is very radical, but compared with the organic changes over the past two centuries, in one fell swoop it forces acquiring authorities to offer a purchase price for properties that will satisfy current owners and so heavily reduce the number of objections and so shorten any inquiries (although clearly this will not influence lobbyists whose concerns relate solely to the environmental aspects of a project).

4. Conclusion

After almost two centuries of legislation and case law surrounding the CPO system, the radical but simple solution proposed in this report would make the issue of CPO compensation more straightforward. It would require one line in a new Act or as an amendment to existing legislation to say that "all compensation is to be [X times] the open market value". It would require politicians and AAs to accept that the current system is opaque and labyrinthine even despite the most recent reforms. By setting down a basic principle over generous upfront compensation it will enable AAs to push ahead with their

plans in the confidence that they have satisfied local property owners and in exchange bought themselves a route to a speedier start to construction work.

Implementation of the infrastructure plans outlined by the government in March just as the coronavirus pandemic was starting to exert its fatal grip on society and the economy could not come at a better time. Much-needed investment in energy, road, rail, housing, and broadband will be easier to achieve under a fast-tracked system. **Now is the time to accept that paying higher compensation today to secure the property needed for major projects will pay multiple dividends by reducing the overall cost tomorrow.** As Benjamin Franklin is reputed to have said: "An ounce of prevention is worth a pound of cure."

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[i] Budget 2020. HM Treasury. 11 March 2020

[ii] The Inclosure Act 1773 (13 Geo 3. c. 81). Parliament of Great Britain; Neighbourhood Planning Act 2017. UK Public General Acts. 2017 c. 20

[iii] Compulsory Purchase and Compensation: Compulsory Purchase Procedure. MHCLG. 26 October 2004

[iv] Ministry of Housing, Communities and Local Government (LVC084) CHECK REFERENCE

[v] https://publications.parliament.uk/pa/cm200102/cmselect/cmproced/823/2070206.htm

[vi] National Infrastructure Planning. The Planning Inspectorate. Website accessed 4 November 2020

[vii] Reacting to a CPO — what do you need to do? Real Estate News. Hogan Lovells. 3 October 2019

[viii] Legal landscape: Land CPOs — a fair price to pay? *The Planner*. 14 March 2019

[ix] Land Value Capture. House of Commons Housing, Communities and Local Government Committee Tenth Report of Session 2017–19. Page 10. 10 September 2018

[x] Towards a Compulsory Purchase Code: (1) Compensation Final Report. The Law Commission. December 2003