

The Community Infrastructure Levy begins to bite – Issues of concern and implications for transactions

After lengthy preparation and many changes of tack by successive governments, the Community Infrastructure Levy (or CIL) has finally come into effect in the first local authority area. Newark & Sherwood DC's CIL came into force on 1 December 2011 and a number of other authorities are preparing to implement their own CIL in the next few months. Developers will gradually need to become familiar with CIL as a major component of the development process. It is also increasingly likely that developers and investors will start to come across CIL in their real estate transactions and they need to be aware of the implications.

CIL will be payable in relation to most forms of development in local planning authority (LPA) areas where it is introduced. It will replace many of the tariff-type payments seen currently in Section 106 agreements towards items such as general road improvements, environmental and education projects. Whilst it is optional for LPAs to implement CIL, they will in practice be forced to do so because changes to Section 106 rules will ultimately prevent them pooling contributions for larger-scale infrastructure projects except through CIL. Having said that, Section 106 agreements will still be required for affordable housing and other direct site impacts, although the government is now considering whether CIL should be extended to some affordable housing provision.

LPAs will set their own rates of CIL based on the amount of infrastructure they assess as being necessary to support development in their area. It will be payable on the net additional amount of floorspace created by new development and varied rates can be set for different types of development and in different zones. For example, retail development in Newark Growth Point will cost £125 / sq m. For the same in Collingham it will cost £100 / sq m. The London Mayor will also be able to charge CIL as a contribution towards Crossrail (on top of any CIL charged

Key issues

- Various issues of process still arise as to how CIL will work
- Developers and investors should consider the implications of CIL for their RE transactions
- A key points summary of CIL is contained in the Annex

by a London Borough), and this is expected to come into force around 1 April 2012. CIL charges of between £20-50 sq m are proposed depending on the borough, for most types of development.

CIL in the development process

CIL will mainly be relevant for the planning and development process itself. We have included a brief summary of how CIL will work in the Annex to this briefing. Some general issues of concern still remain in relation to how CIL will operate, including the following:

- Developers will need to keep an eye on the progress of CIL proposals. A planning application will only escape from CIL if the permission is issued before CIL comes into effect; if the permission has not been formally

issued, CIL would still apply. Consideration should be given to whether Section 106 agreements should incorporate some form of credit to be given against CIL payments to deal with such circumstances. This is particularly important given that applications to vary a permission under Section 73 of the Planning Act 1990 will be caught by CIL. The absence of such provisions in Section 106 agreements could well lead to double-charging.

- There is no obligation or timetable imposed on the LPA to provide specific infrastructure to be funded from CIL receipts. Where additional infrastructure is seen as key to a development, a developer may be forced to

"a planning application will only escape from CIL if the permission is granted before CIL comes into effect."

fund it under a Section 106 or other agreement rather than wait for the authority to carry out necessary improvements. Again, this creates a potential for double-charging.

- The recently passed Localism Act requires a "meaningful proportion" (yet to be defined) of CIL payments to be passed on to neighbourhoods to fund infrastructure or other development-related needs; this could lead to further pressure on the timing for LPA infrastructure projects or whether they be provided at all.

Transaction implications

The principal implications of CIL for real estate transactions result from the following issues:

Fallback owner liability

The CIL regulations allow anyone to assume liability for CIL on a project but where no-one does or there is a default, the owners¹ will be liable based on the value of their relative interests.

Landowners, tenants and developers involved in development transactions (e.g. through development agreements or other agreements conditional on planning

being obtained) will want to ensure, among other things, that the assumption of CIL liability is clearly dealt with in the documents. The parties would be well advised to deal with these issues even where the agreement is signed before CIL takes effect in an area, to cover the eventuality that CIL is introduced before planning permission is obtained.

As and when CIL is introduced in an area, buyers / new tenants or lease assignees will need to be aware that any unpaid CIL relating to development already carried out could be imposed on them. Price adjustments or other contractual protection may be necessary in these cases.

An additional issue arises for leases: a tenant could incur CIL liability for future development by its landlord even if the tenant does not consent to such development being undertaken (and vice versa). Where a new lease is being granted, this presents an opportunity to protect both parties from taking on any such liability.

Co-existence of Section 106 Agreements and CIL

This issue is relevant to development transactions. Since Section 106 agreements and CIL payments are likely to co-exist, the parties will also need to factor in both types of payments to the costs of the development, for example when determining whether planning gain requirements are "onerous". Again the parties should deal with these issues even before CIL has taken effect in an area.

Social Housing relief

Various reliefs are available against CIL liability. Where qualifying social housing is provided as part of a development (e.g. as on-site affordable housing in a mixed use development), social housing relief applies and no CIL is therefore payable. Significantly, this relief could be withdrawn (and CIL would become payable retrospectively) if the housing ceases to be used for social housing within a 7 year period². Depending on the circumstances, either the Seller or the Buyer of land benefitting from relief could be hit with this charge, and sale price amendments or other contractual protection may be required.

¹ See Annex for further details.

² See Annex for further details.

Final Comments

The framework, calculations and procedures for CIL are not straightforward. We have set out a brief summary of how CIL works in the Annex to assist in getting to grips with the basics. The major additional recommendation to

developers and investors is to follow the CIL progress of the London Mayor and of local authorities in areas relevant to your projects and proposed acquisitions. This will help to ensure that CIL does not bite unexpectedly.

Annex - How CIL works – Key Points

The regime for CIL is provided under the Planning Act 2008 and the Community Infrastructure Levy Regulations 2010 (as amended) and applies in England & Wales.

How will CIL be set by charging authorities?

Charging authorities will set CIL based on the amount of infrastructure required to support development in the area concerned. Differential CIL rates can be charged for different types of development or for development in different zones (but only based on development viability criteria). Tariffs must be set as [X] £ / sq m gross internal floorspace. Payment of CIL is then subject to indexation.

Responsibility to pay CIL

Which Developments?

Subject to a few exceptions, discounts and a threshold of 100 sq m of development, CIL will be chargeable on the development of most types of buildings (whether express permission is required or not).

CIL is only chargeable on the net increase in floorspace although there are complicated provisions to identify whether existing floorspace can count to reduce CIL liability.

CIL will only be chargeable on development under planning permission granted after a Charging Schedule has come into effect.

When is CIL on a development valued?

CIL, index-linked from the time the Charging Schedule was put in place, will be applied to a development based on the date it is "first permitted". For a full permission, this is the later of the grant of planning permission and satisfaction of the last remaining condition needing to be satisfied before commencement of development. For an outline permission it is the grant of approval in relation to the last remaining reserved matter. Where permissions are phased, this results in separate CIL charges for each phase of the development.

Developers relying on Permitted Development rights will be required to serve a "Notification of Chargeable Development" before they carry out the development. This will crystallise the CIL charge.

Who is liable?

Anyone can assume liability for CIL but where no party does so (or there is default), the owners will be liable based on the value of their land interest (and surcharges may be applied). The owner is any freeholder and any leaseholder with over 7 years of lease term remaining at the time the development is first permitted. A person who has assumed liability can transfer liability to another person at any time before the final CIL payment becomes due.

Reliefs

Various reliefs exist for charities, social housing provision and exceptional circumstances.

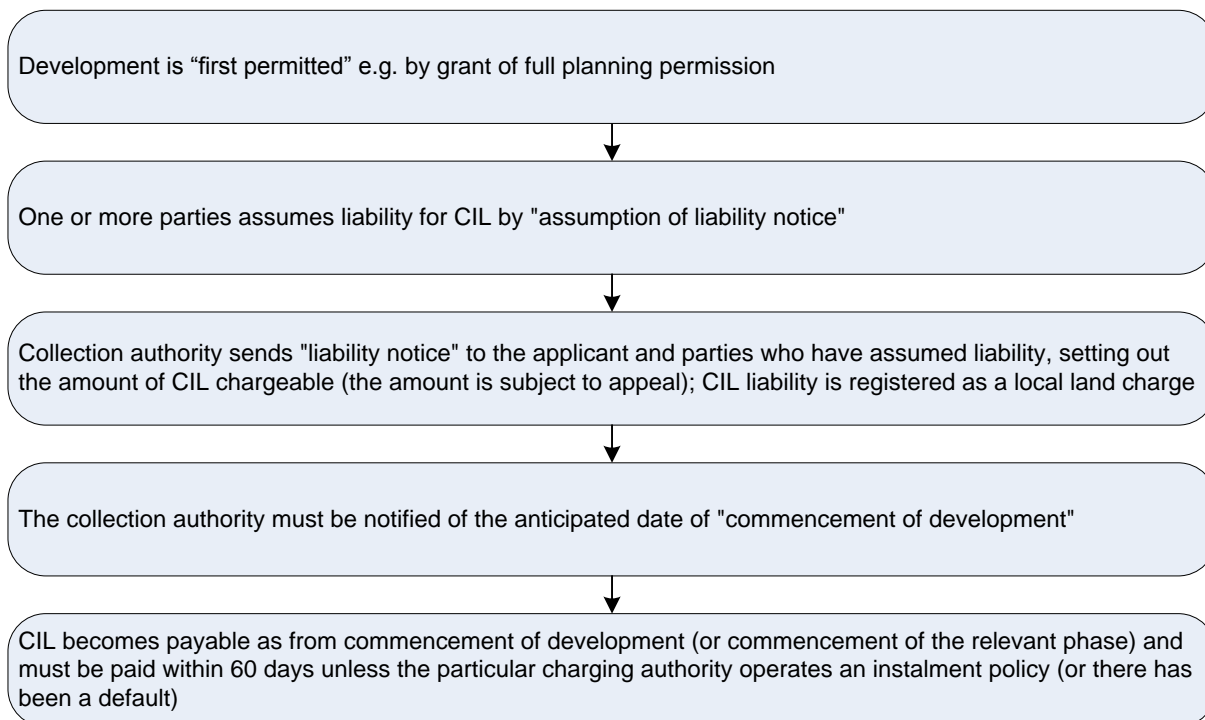
Where charging authorities choose to adopt it, "exceptional circumstances relief" is a discretionary relief from CIL based on evidence being provided that the development would not be viable if full CIL payment was made.

Social Housing Relief applies for the development of qualifying social housing. This includes: social rented housing; intermediate rental housing (up to 80% of market rent); and shared ownership lease arrangements where the initial premium payable does not exceed 75% of market value with limits on further rent. Social Housing Relief is subject to clawback if, within a 7 year period, dwellings cease to be qualifying social housing. Clawback is from the original applicant for relief except where the housing has been sold before occupation in which case the clawback is from the buyer.

There are complex provisions relating to entitlement and procedures for applying for such reliefs.

The CIL payment process

Broadly speaking, CIL payment works as follows:



Where a planning application has been made in relation to a site incorporating several plots (such application requires no ownership interest), commencement of development on one plot could cause CIL to be imposed on other plot owners without their consent. A "suspension of demand notice" procedure may help to prevent an innocent plot owner having liability unknowingly imposed on them.

Payment in kind

CIL can be satisfied (in whole or part) by payment-in-kind but only to the extent that such payment is made through the transfer of land to the authority (or to a third party nominee) to be used for infrastructure purposes, a so-called "land payment".

There are various conditions including that the amount credited against CIL liability is the independently assessed market value of the land. Land payments have to be made within the relevant instalment timetable.

An agreement to make a land payment must be made before the development is commenced. Although this cannot be a Section 106 planning obligation, it is as yet unclear whether, for convenience, the relevant provisions could still be contained within a Section 106 agreement as a standalone provision.

Enforcement

Various new powers are given to collecting authorities to deal with non-payment of CIL and other breaches of the provisions. These include, in particular, a CIL Stop Notice which can require development to stop if CIL has not been paid. Failure to comply with a CIL Stop Notice would be a criminal offence.

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