Dear Sir/Madam

Compulsory Purchase Interest Rates

Through the Housing and Planning Act 2016 and Neighbourhood Planning Act 2017, the Government has introduced a package of reforms to make the compulsory purchase process clearer, fairer and faster for all. Most recently, we introduced measures to streamline the decision-taking process for compulsory purchase orders and enable earlier advance payments of compensation, both of which came into force on 6 April 2018. We also published updated compulsory purchase guidance, which was revised to reflect the reforms introduced since 2016.

As part of this wider reform process, the Government previously consulted on amending the interest rate arrangements for compulsory purchase in order to incentivise swifter payments of compensation. This included an improved rate on outstanding compensation and the introduction of a new penal rate of interest where advance payments are not made on time. These measures have not yet been implemented. The Government has reflected further on the possible unintended consequences of the previously proposed rates, and believes that additional consideration of potential gaming risks is required.

Through this targeted engagement exercise we are seeking initial views on the extent of potential gaming risks of previous reform proposals, and possible measures to address such risks. The note at Annex A outlines the Government’s concerns in more detail and poses a series of questions, which we would be very grateful to have your responses to. A response form is enclosed with this letter. If you wish to respond, this should be completed and sent to: CPOInterestRates@communities.gsi.gov.uk by 12 June 2018.

This letter has been sent to the organisations listed at Annex B, which includes – but is not limited to – those who responded to the interest rate proposals consulted on in March 2015 and March 2016. However, we are content for you to share this letter with others who may have an interest in this matter and wish to respond. All the responses to this targeted engagement will be carefully considered, and a Government response will be issued.

Yours faithfully,

Tom Winter
MHCLG Planning Directorate: Development Management

May 2018
Annex A

Further Consideration of Compulsory Purchase Interest Rates

Background

1. After a compulsory purchase order (CPO) has been confirmed it can take time for the acquiring authority and claimants (i.e. those with an interest in the Order Lands) to agree on the amount of compensation due. Claims may not always be settled and/or paid until after the acquiring authority has entered and taken possession of the land. In this scenario, claimants may need to finance their own relocation costs – potentially by taking out a bridging loan. This can exacerbate the stress and inconvenience of being subject to a CPO.

2. To address this situation, claimants can request an advance payment of compensation prior to the final amount being settled. An advance payment is 90% of either the amount of compensation agreed between the parties or the acquiring authority’s estimate of the total compensation due. An advance payment must be made if one is requested by a claimant. However, there is currently no sanction where advance payments are made late – or not at all.

3. Whether or not an advance payment is made, there may still be an outstanding amount to be paid (potentially a significant amount if no advance payment is claimed and/or made). To compensate for such delays, simple interest is payable on any outstanding balance of compensation from the date on which the acquiring authority enters and takes possession of the land. The current rate is set at 0.5% below the Bank of England (BoE) base rate (with a floor of 0%).

Previous Reform Proposals

Outstanding Compensation

4. Since March 2009, the BoE base rate has been 0.5% - falling to 0.25% between August 2016 and November 2017. As such, the effective rate of interest payable on outstanding compensation during this period has been zero. This provides little financial incentive for acquiring authorities to settle compensation claims promptly. Furthermore, the longer payment is delayed, the more the value of the compensation diminishes in real terms, as no interest is paid to keep up with inflation. It is reasonable to assume that claimants in receipt of their compensation would invest it in some form – whether a new property or a savings account – all of which would have an anticipated return above 0%. As a result, the current situation can ultimately leave claimants out of pocket.

5. In March 2015, the Government consulted on changing the prescribed interest rate to 1% above the BoE base rate. In its response to that consultation, published in October 2015, the Government stated its intention to take forward a rate of 2% above the BoE base rate. HMT is responsible for making the regulations that would give effect to any change to the relevant rate.

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1. Under section 11(1) of the Compulsory Purchase Act 1965
2. At the rate prescribed by regulations made by HMT under section 32 of the Land Compensation Act 1961
3. The Acquisition of Land (Rate of Interest after Entry) Regulations 1995 (as amended)
Advance Payments

6. Given the support they offer to claimants, not least in helping to finance relocation, there is clear benefit in advance payments being made as swiftly as possible. This can help to reduce the stress and disruption that compulsory purchase can cause. The Government’s March 2015 consultation contained a number of proposals to make the process of obtaining an advance payment fairer and faster. The proposals included allowing advance payments to be claimed and made earlier, introducing a claim form and setting time limits on requests for additional information.

7. The October 2015 Government Response confirmed that these measures would be taken forward, and the relevant provisions were included in the Housing and Planning Act 2016. Although a power to prescribe a statutory form was taken as a back-stop, it was decided to initially publish a voluntary claim form which was done on 22 September 2017. New provisions governing the timing of advance payments were commenced on 28 February 2018, and came into force on 6 April 2018.

8. The October 2015 Government Response also confirmed that it would take a power to set a penal rate of interest as a sanction against late advance payments. This is contained in section 196(3) of the Housing and Planning Act 2016. A separate consultation published in March 2016 proposed setting a rate of 8% above the BoE base rate, which the subsequent Government Response (September 2016) suggested would be taken forward. As with the rate of interest that applies to outstanding compensation, HMT is responsible for making regulations that set the rate of interest for late advance payments4.

Further Consideration of Gaming Risks

9. Neither of these interest rate proposals has yet been taken forward. As noted, the Government has reflected further on the possible unintended consequences of the previously proposed rates, and believes that additional consideration of potential gaming risks is required. We want to hear stakeholders’ views on these matters before finalising our proposed approach. The Government’s concerns are outlined below.

Outstanding Compensation

10. The intention behind introducing an improved interest rate for outstanding compensation is to encourage speedier compensation payments, whilst also ensuring claimants are not unduly disadvantaged – in real terms – where compensation is not paid in a timely manner. We want to ensure the arrangements are fair to both acquiring authorities and claimants.

11. The Government’s concern, however, is that an interest rate of 2% above BoE base rate could – in certain circumstances – have the unintended consequence of disincentivising claimants from seeking to agree compensation as swiftly as they might. Specifically, it could create a scenario in which some claimants instead seek to maximise the outstanding amount of compensation (on which the proposed new interest rate would be accrued) for the maximum amount of time. To engage in such ‘gaming’ a claimant could, for example, decline to make

4 See section 196(3) of the Housing and Planning Act 2016
either a claim for compensation in response to a notice to treat/general vesting declaration, or a claim for an advance payment and simply wait for the matter to be referred to, and determined by, the Upper Tribunal.

12. The motivation to pursue such behaviour could arguably arise if an interest rate of 2% above the BoE rate exceeds the returns that a claimant could obtain from ‘risk free’ investments elsewhere.

13. To the extent that there could be a gaming risk, we anticipate it being restricted to a minority of cases. That is because regardless of what the interest rate on outstanding compensation is, we expect that the majority of claimants will be keen to settle compensation claims as quickly as possible so they can put their affairs in order. Gaming of this type is only likely to be contemplated by those in a financial position to forego compensation for a prolonged period without this having a material impact on their business or livelihood. Even so, the potential amount of interest at stake could potentially be substantial – for example, with a large site in a city centre. This could have significant fiscal implications for acquiring authorities, and in turn, the cost of delivering taxpayer-funded projects. We are therefore keen to understand the extent of potential risk.

**Question 1:** Do you think that an improved interest rate of 2% above Bank of England base rate could incentivise some claimants to ‘game’ the process by prolonging negotiations in order to maximise their interest entitlement?

**Question 2:** If so, how widespread do you think such practice might be and what might the scale of financial impact be for acquiring authorities?

14. As to potential mitigation measures, we do not believe there is currently an **absolute** safeguard if claimants did indeed seek to prolong negotiations for the sole purpose of maximising interest payments in the light of an improved rate.

15. One potential option might be for Government to issue additional guidance on how it expects claimants and acquiring authorities to engage in the process of negotiating compensation. This could clarify that the express purpose of the interest rate for outstanding compensation is to encourage swift payments, and in that context, underline that it is not considered reasonable for claimants to prolong, or disengage from, compensation negotiations simply to maximise interest. While it is recognised that such guidance would not necessarily prevent gaming, it could help to discourage such a practice given that it could potentially be taken into account by the Upper Tribunal in deciding whether to award costs against parties for unreasonable behaviour.

16. Going further, and if the evidence suggests a statutory safeguard is required, we could consider potential legislative options. For example, such options might involve amending legislation to:

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5 Under Section 29(4) of the Tribunals, Courts and Enforcement Act 2007 or Rule 10(3) of the Tribunal Procedure (Upper Tribunal) (Lands Chamber) Rules 2010.

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• Provide for acquiring authorities to make advance payments even where no claim for one has been made (i.e. to reduce the amount of outstanding compensation).

• Provide for acquiring authorities to pay money into court where a claimant has refused to accept a payment.

• Provide that interest is not payable on compensation that is offered but not accepted by a claimant.

17. The above are very preliminary proposals. If legislative interventions were deemed to be necessary in the light of stakeholder feedback, any such proposal would need to be subject to detailed policy development and further engagement.

18. Since 1995 the interest payable on outstanding compensation has been expressed as a fixed percentage relative to the Bank of England base rate. A potential alternative approach could be to set the relevant rate (for the purposes of Section 32 of the Land Compensation Act 1961) by reference to a fixed multiplier. This would involve prescribing a rate of, for example, 1.5x, 2x or 3x the Bank of England base rate. We would be interested in hearing your views on taking such a multiplier-based approach, and whether it would offer any material advantages over the current approach of using a fixed percentage.

Question 3: What, if any, measures do you think might help to reduce the risk of – and scope for – gaming of the interest provisions for outstanding compensation?

We would be interested in your views on the options outlined in paragraphs 16-18, as well as any other suggestions you might have.

Advance Payments

19. The intended purpose of introducing a penal rate for late advance payments is to provide a strong incentive for acquiring authorities to pay on time where one is requested. This recognises the vital role of advance payments in supporting claimants prior to the final amount of compensation being settled.

20. We do not consider that the potential risk(s) of gaming identified in relation to outstanding compensation would arise in this context. That is because it will be within the gift of acquiring authorities to ensure that the penal interest does not arise – by paying an advance payment on time. Indeed, ensuring timely payment was the stated policy objective of introducing a penal rate.

21. We remain committed to introducing a penal rate of interest for advance payments that are paid late. However, having reflected further, the Government is concerned that although businesses can charge ‘statutory interest’ of 8% above the BoE base rate if another business is late paying for goods or services, this is unprecedented in the context of compulsory purchase. A number of respondents to the previous consultation – not just acquiring authorities – suggested this figure was too high.
22. We are interested in hearing further views on whether the Government’s objective could be realised through a lower rate than was previously proposed – for example, 4% above the Bank of England base rate.

<table>
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<tr>
<th>Question 4: Could the policy objective of strongly incentivising timely advance payments be achieved by setting a lower penal rate than 8% above the Bank of England base rate? If so, we would be interested in your views on potential alternative rates.</th>
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Annex B

List of organisations invited to comment

Accessible Retail
Aylesbury Leaseholders Action Group
Bedford Borough Council
Berkeley Group
Birmingham City Council
BNP Paribas Real Estate
Bond Dickinson
Bristol City Council
British Property Federation
Browne Jacobson LLP
Building Societies Association
Caxtons
Central Association of Agricultural Valuers
Compulsory Purchase Association
Country Land and Business Association
Devon County Council
Doncaster Metropolitan Borough Council
EDF Energy
EMEPF
Empty Homes UK Ltd
Energy UK
EY
Falcon Chambers
Fisher German

Greater London Authority
GVA
Hartlepool Borough Council
Highbury Group on Housing Delivery
Highways England
Historic England
Homes England
HS2 Ltd
Kent County Council
Law Society
Local Government Association
London Borough of Southwark
National Farmers Union
National Grid
National Infrastructure Planning Association
Norfolk County Council
North Norfolk District Council
Nottinghamshire County Council
Peter Brett Associates LLP
Planning and Environmental Bar Association
Planning Officers Society
RiverOak Investment Corporation
Royal Borough of Kingston upon Thames
Royal Institution of Chartered Surveyors
Royal Town Planning Institute
Savills
Sawyer Fielding
Seven Trent Water
Shakespeare Martineau
Shelter
South Norfolk Council
Stoke-on-Trent City Council
Swindon Borough Council
Tanner Rose LLP
Tatton Estate Management Ltd
TLT LLP
Town and Country Planning Association
Town Centre Regeneration Ltd
Transport for London
UK Finance
Wessex Water
Yorkshire Water