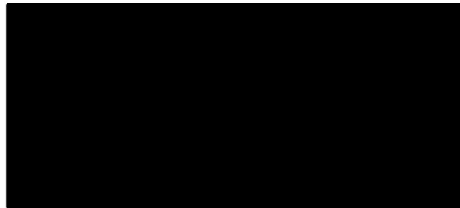
WAVERLEY COUNCIL



Our ref:

5 August 2020

NSW Productivity Commissioner
Submitted via email to
ICReview@productivity.nsw.gov.au

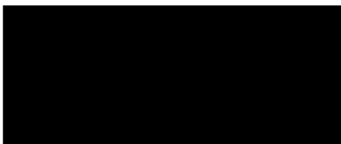
Waverley Council Submission to the Productivity Commissioners *Review of Infrastructure Contributions in NSW*

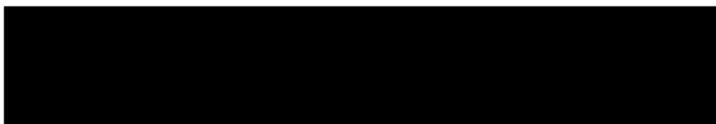
We wish to thank the Productivity Commissioner (PC) for allowing Council to make this submission to the *Review of Infrastructure Contributions in NSW (PC Review)*.

This submission is structured based on the discussion questions from the PC Review. The submission argues that value capture mechanisms should be formalised and accepted as part of the VPA framework, but should be broadened to include a betterment levy across all upzoned land in NSW and mechanisms to capture value uplift associated with major public investment in infrastructure.

Should you have any questions about the contents of this submission please contact

Regards,





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General feedback on 'Housing undersupply and declining approvals' section

This PC Review references the argument about an 'undersupply' of 100,000 dwellings and suggests that constrained supply, combined with lower interest rates, "helped propel an unprecedented uplift in housing prices over the past decade". House prices are driven by a range of factors, including but not limited to, underlying demand from a changing population compared to housing supply, as well as household incomes and interest rates (influencing effective demand). However, investor sentiment, favourable taxation settings and other cyclical factors mean that housing prices are not the best way to tell if supply and demand are in balance. Arguably the cost of renting a home, rather than buying, is in some ways a better indicator of whether supply is meeting demand.

Using rents as an indicator of the supply-demand relationship will give a clear picture of the real 'need' for housing as shelter. Using house prices as an indicator – as governments, developer lobbyists and analysts have done – distorts the picture as it includes the asset price inflation boom that more accurately reflects the 'want' for housing as an investment vehicle.

There is no undersupply of housing in Sydney – this is a myth
Notwithstanding the commendable analysis, the PC Review perpetuates the ongoing 'supply myth' by purporting that there is a significant undersupply of housing in Greater Sydney; which tends to be followed by a logic that planning reforms are needed to address this undersupply.

The PC Review should indicate the notion that Greater Sydney had an 'undersupply' is a claim and not fact. If it is true that rents are an accurate indicator of the balance of supply and demand, and rents have grown at the same rate as inflation for the past decade and more, how can there be an undersupply of 100,000 homes in Sydney? If there was such a large and persistent undersupply of housing, then rents would have grown at a much faster rate than CPI and in line with house price growth. The arguments being made on undersupply are based on house prices and the belief that the two house price booms since the 2000s have been based on a lack of supply. Research from the RBA indicates that house price increases in Sydney and Australia have been driven by interest rate falls, along with record high immigration.[1] The RBA study shows that a 1 per cent drop in interest rates will increase prices by 30 per cent, but a 1 per cent increase in the number of dwellings only lowers house prices by 2.5 per cent. Given that new housing supply only adds just over 1 per cent to housing stock each year, even a doubling of housing supply would have a negligible impact on house prices where these are set by *all house sales*, existing and new supply.

The story housing supply in Sydney is a great success
Housing supply in Sydney has one the highest dwelling completions rates in the developed world. Sydney is currently producing more dwellings than London (32,000), despite having a population less than half. Australia is producing housing faster than any other OECD nations at 8.2 completions per 1000 persons, up from 6.8 in 2010. In the most recent residential construction boom, there were more cranes servicing apartment construction on the east coast of Australia than in major cities across North

[1] Saunders, T & Tulip P, 2019, 'A Model of the Australian Housing Market', Research Discussion Paper 2019-01, RBA

America, including New York, Boston, Chicago, San Francisco, Los Angeles, Toronto and Calgary. Fifty per cent of all cranes in the east coast of Australia were in Sydney. Sydney's dwelling production peaked at 45,000 dwellings a year in 2019 – 36 per cent higher than the previous peak in 1970 – and approvals peaked at 60,000 dwelling approvals per annum in 2019.[2]

In the short to medium-term there is an abundance of approved and ready to develop greenfield and infill sites in Sydney, with 190,000 dwellings in the pipeline in the next five years. This is an 8 per cent increase compared to the last five years, which was the largest approvals and construction boom in Sydney's history. Since 1999, the cumulative gap between approvals and completions is 142,000 in Sydney alone, with over 100,000 surplus approvals granted since the 2012 price boom began3. These were also the highest rates of housing supply in the world. The historical patterns of new dwelling supply and population growth show that there has also been a surplus of new dwellings when compared to historical patterns of new dwelling supply and population change.[4]

General feedback on role of 'contribution capping' and supply

The PC Review notes that the development contribution caps were put in place to "sustain housing supply amidst the 2008-09 Global Financial Crisis and were aimed at stimulating construction". However, the fall in supply was a result of a drop-off in aggregate demand, not issues with supply costs. There is strong anecdotal evidence in the greenfield areas of Sydney which demonstrate that 'overnight' after the introduction of the caps, landowners increased their asking prices to absorb any saving from the cap. The PC Review does correctly acknowledge this phenomenon: "*over time it is likely that these subsidies were ultimately taken up in terms of higher land values."*

There should be greater emphasis in the final PC Report that the supply pipeline is led by the market and the number of applications being submitted by the development industry. If supply drops that's because market conditions are not right (interest rates, foreign investment, migration etc.) and developers have stopped lodging development applications. Approvals dropped, but not approval *rates*. No one was buying, so no one was building, so no one was putting in applications, so there were less approvals and less completions. That is not a problem with the contributions being too high.

Issue 1.1: Striking the right balance

There can be difficulty in reconciling the competing principles of efficiency, equity, certainty, and simplicity. Failure to strike the right balance can undermine confidence in the planning system.

Is a 'one size fits all' approach appropriate or do parts of the State require a bespoke solution?

A standard percentage rate betterment (value uplift) levy should apply across the state. This approach automatically adjusts to local market conditions and ensures that the levy does not change the

[2] Sneesby, T 2020, 'Fast-tracking development in NSW: genuine reform or rent-seeker give-away?,' The Fifth Estate, accessed 12 July 2020

[3] Sneesby, T 2020, 'Don't blame planning for a supply shortage and rising house prices,' The Fifth Estate, accessed 12 July 2020,

[4] Murray, C 2019, 'The Australian housing supply myth.'

feasibility of a site for development. No bespoke solutions are necessary. A betterment levy would tick all boxes of efficiency, equity, certainty and simplicity.

Where the value gain from a change of use is small, the betterment levy is lower (it is a fixed rate on the small gain), and where the value gain is large, the betterment levy is higher (again, a fixed rate, but now on a higher value gain). To the extent that a betterment levy would be a fixed rate, then it would in a way be a bespoke solution, whereby a higher contribution would be levied in areas where contributions are typically high to pay for land acquisition costs.

It also means developers would never get stuck with unanticipated SIC (or other) contributions that render their approved development infeasible, especially in marginal cases where value gains from redevelopment are low. Developers would never 'overpay' for a site and indeed, the more a developer 'overpays' the greater funds that are raised for infrastructure contributions.

Like has occurred in many parts of the ACT, betterment levies can be pre-calculated based on typical betterment values in different local precincts where redevelopment is desired in the planning scheme. This further reduces uncertainty in areas where development is desired in the planning scheme, and reduces the number of times individual assessments of betterment are required

If a Betterment levy raises more money than required to fund infrastructure, then the NSW Government could recycle and hypothecate this back to the provision of affordable housing in the area.

An alternative and less drastic change to the NSW contributions system could be that a lower betterment levy apply across the board and that a bespoke solution, such as a 7.11 plan, would be additive to this broad rate.

What are the advantages and disadvantages of a site-specific calculation based on demand generated, compared with a broader average rate?

Site-specific is more equitable as it creates a price signal and reduces cross-subsidisation of infrastructure funding. However, if a betterment levy is applied on uplift, then this has the advantage of a broad rate that everyone knows and is site-specific.

From an efficiency point of view, infrastructure costs should create a price signal to direct development to occur in areas where it is most viable – allocating resources to their best use. By supporting an economically efficient outcome, we ensure areas with higher costs of delivery will have this reflected in charges.

From an equity point of view, service delivery and cost apportionment should be treated consistently across service types, locations, and levels of government. Costs should not be borne by parties that are neither an impactor or a beneficiary. Consistent treatment builds confidence in the planning systems.

Do other jurisdictions have a better approach to infrastructure funding we should explore?

The ACT has a 75% Betterment levy called a 'Lease Variation Charge' that is best practice (more detail on this elsewhere in this submission).

Issue 3.1: Principles for planning agreements are non-binding

The Planning Agreements Practice Note is currently non-binding on councils, although the Ministerial Direction exhibited by the Department aims to change this. There are no equivalent guidelines for use when negotiating planning agreements with the State. Additionally, there is little agreement between stakeholders on what the principles should be for either local or State planning agreements and there is no consensus on the appropriateness of value capture through planning agreements.

What is the role of planning agreements? Do they add value, or do they undermine confidence in the planning system?

To add value VPAs should be linked to a Council's strategic infrastructure planning and funding framework. The current and draft Practice Note already states that Planning Agreements should not be used as a revenue raising exercise to overcome spending limitations or for improper use and should not be 'wholly unrelated' to development. The evidence suggests that funds from Planning Agreements are hypothecated towards public infrastructure that has a link to the development in question.

In addition to being explicitly linked to Councils infrastructure funding plans and policies, there may be circumstances that arise where a development can contribute new infrastructure. This could be in the form of an adjacent park, affordable housing or other community infrastructure that may be consistent with the Local Strategic Planning Statement or other projects and priorities as outlined in Council's suite of urban policies and strategies.

A set of policy principles for Planning Agreements for guiding councils and other stakeholders could include:

- Meeting the needs of a growing population with infrastructure that improves local public amenity and liveability
- Acting in the public interest
- Supporting economically viable development
- Linking the planning agreement process and the delivery of public benefits
- Fairness for all parties with decisions based on merit and ensuring the agreement is actionable
- Independent performance of statutory functions and commitment to published planning strategies and the application of gazetted planning controls
- Transparency in decision-making and reporting where flexibility and trade-offs are involved
- Acting to dampen speculation in land and enhance housing affordability
- Testing decisions using public exhibition of planning proposals and development applications and public consultation
- Adherence to published policies, practices and accountabilities that maintain probity and ensure conflicts of interest are mitigated.

Such a set of governing principles then enable councils and proponents to safely navigate a potentially complex issue to a desired outcome that is in the public interest. As public policy they would assist with countering perceptions about planning decisions being bought and sold.

Is 'value capture' an appropriate use of planning agreements?

Yes.

Until the Government introduces a broad based value capture scheme, such as a betterment levy, which returns to the community a fair share of any unearned land value uplift resulting from planning decisions that currently flows fully to landowners, it is reasonable and valid for Planning Agreements to be a mechanism to achieve this purpose. Waverley has been implementing a value capture based VPA policy since 2012 and that the vast majority of VPAs are from local developers who understand and have been involved in the development of the system given the certainty it provides in their feasibility.

The case for VPAs functioning as a betterment levy is particularly important in inner-city areas, where a traditional s7.11 (formerly s94) is difficult to apply because the principles of 'nexus' and 'apportionment' are too difficult to calculate. Therefore, a number of inner-city Councils rely on the s7.12 (formerly 94A) 1% levy which is inadequate to keep up with the infrastructure needs in these areas.

In this context, the current infrastructure funding arrangement results in the costs of growth being borne by existing residents, while the benefits of growth accrue to few landowners in the form of a windfall gain. Arguably this disparity has been one factor that has led to a reduced 'social licence' for new development in existing urban areas.

A value capture approach acts as an 'informal nexus', whereby upzoned areas generate new demand (in the form of additional development rights) and this demand is linked to the value capture mechanism, which can fund major upgrades.

The recently released DPIE draft Practice Note aims to remove value capture as key consideration purporting to respond to recommendations from the Kaldas Review. The Kaldas Review did not state or even imply that the value capture approach should be abandoned. This review made only the following recommendations relating to VPAs**: u**nderpin VPAs with proper strategic infrastructure planning, delivering on the commitment to community to provide appropriate growth infrastructure; ensure identified infrastructure reinforces the link between public benefit and the proposed development, and must not include additional, unrelated items sought by local councils; prevent Council from requiring a VPA to progress a planning proposal – planning decisions cannot be bought or sold; and, ensure transparency, compliance and accountability.

The removal of the explicit use of value capture in VPAs is based on a number of 'myths', as outlined in summary below, and in more detail in other sections of this submission.

- **Myth: Value capture doesn't have a nexus**: upzoned areas generate new demand and this demand is directly and proportionally linked to the value uplift.
- **Myth: Value capture incentivises conservative (low) planning controls:** Councils are required to update their controls based on housing and employment targets and housing strategies.
- **Myth: Planning Agreements slow down housing approvals:** developers do not have to offer VPAs and VPA negotiations can occur concurrently with the DA Assessment process to ensure a timely response.
- **Myth: Value capture costs are 'passed on' to the home buyer:** The price of dwellings is determined by the market – the balance of supply and demand.

- **Myth: Value capture undermines strategic land use planning:** developers have always had discretion to exceed existing controls before value capture. Value capture lowers the economic payoffs to private landowners, distributes it to the community and reduces the incentive for developers to 'capture' the system in order to have it deliver them a windfall.
- **Myth: Value capture can lead to planning decisions being bought:** Value capture simply means Councils are putting a price on additional floorspace that would otherwise be given away for free. DAs or PPs go through a rigorous and independent assessment process, which eliminates the possibility for decisions being bought.
- **Myth: Value capture holds developers to ransom:** it is a developers choice to exceed the existing planning controls.
- **Myth: Value capture is simply a 'cash grab'**: VPAs are often linked to strategic funding opportunities identified in a Capital Works Program/relevant Council policy or benefit residents of the new development.

VPAs are the only mechanism available in NSW to share in land value uplift. Spot rezonings and clause 4.6 variations are an established part of the NSW planning framework. If a value capture approach to uplift is ruled out, then developers will continue to exceed planning controls while the public will be unable to share in the uplift through publicly granted development rights.

Should planning agreements require a nexus with the development, as for other types of contributions?

By linking increases in density to infrastructure improvements, value capture not only ties increased demand generated by additional persons, but also links the planning externalities associated with additional development to improved or at least maintained levels of liveability. Hence value capture creates a connection between increased development and liveability. The importance of this connection or nexus cannot be understated, particularly given the NSW Government's intentions to accommodate further growth in existing urban areas.

For more information see heading under Issue 4.2 below: *'Value capture creates a nexus between density and liveability'*.

Issue 3.2: Transparency and accountability for planning agreements are low

Reporting and accounting requirements for planning agreements are low, although proposed changes to the Regulation may improve this. Differing practices between councils and the State in maintaining separate planning agreement registers and public notice systems is confusing and reduces transparency and accountability.

Should councils and State government be required to maintain online planning agreement registers in a centralised system? What barriers might there be to this?

It is noted that Councils are already required to maintain a planning agreement register and most Councils have an online register. Waverley supports a simple online planning agreement register in a central system or on Council's website. Improved reporting on funds received and spent overall is supported to create more transparency and accountability.

Issue 3.4: Contributions plans are complex and costly to administer

Contributions plans can be opaque, making it hard for developers to calculate a potential contribution liability and the community to know what infrastructure it can expect and when. Many plans are not updated in a timely manner, leading to issues with cost escalation, outdated assumptions, and difficulty meeting community infrastructure needs. Some councils have significant contributions balances, indicating there may be barriers to timely expenditure.

How can certainty be increased for the development industry and for the community?

Timing and sequencing of rezoning, utility provision and the delivery of key economic and social infrastructure must be incorporated in an integrated growth plan to achieve the timely supply of the range of housing stock needed to meet the desired land use outcomes.

Contributions obligations need to be made known as a package at the very time growth area structure plans are released for comment. Local, state infrastructure and also any affordable housing contribution imposts need to be known up front to be effective. At least indicative levels of State and local contributions and any value sharing arrangements must be made public at the same time as structure plans for a growth area are publicly released. The charges should be predictable for land purchasers so that the full fair share of any value uplift created by subsequent rezonings is returned to the new community through infrastructure upgrades.

Greater certainty for infrastructure and network planning is provided where agencies can anticipate development patterns. Out of sequence development could be allowed subject to an appropriate and larger amount being paid to address costs arising from the departure from the least cost pattern of development.

It is important to promote reform that improves the transparency and predictability of the amount of all development contributions payable and send a market signal for the desired form and location of development.

Notwithstanding the uncertainty associated with older contributions plans, Council contributions schedules are generally published and some Councils even have calculators – so these are 'certain' and known upfront. Developers often create their own 'uncertainty' when they buy sites that are outside of the strategically planned areas, which don't have contribution schedules or SICs and it can be easy to pay too much if you use a contributions benchmark for an area which is contiguous to infrastructure. There is significant speculating that occurs in Greenfield areas, as outlined in this AFR quote:

> "To secure these large sites, groups would often form a syndicate, then approach potential vendors – typically former farmers – and make an offer, often at excessive prices and on unrealistic terms. This created excessive expectations among vendors, Mr Walsh observed, resulting in reliable offers from developers aiming to secure a site for fair value being excluded.[5]"

What is often not known upfront is the level of State Infrastructure Contribution (SIC). There have been a few precincts (e.g. Parramatta Light Rail corridor) where a SIC rate has been announced concurrently with the land use plan, but this has been rare. And there are question marks regarding the sufficiency of the amount.

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[5] https://www.afr.com/property/commercial/residential-greenfield-land-speculators-predicted-to-lose-big-as-market-softens-20181207-h18vkn

What has tended to happen is that the structure plans are exhibited, and the owners of land proposed to be up-zoned sell land to developers (or speculators) on the legitimate expectation that the Government will not impose more than a token contribution amount on the future developments. The landowners thus pocket all the windfall that comes with up zoning, leaving no room for the developer or community to receive some share of the value uplift to allow it to be reinvested in infrastructure upgrades.

Every element of the metropolitan plan with an implementation horizon of say 5 years should identify the funding sources which will amount to 100% of the estimated implementation cost. This will require agencies such as Treasury and RMS for example, to be involved in the preparation and 'sign off' of the plans. State Treasury should be required to be involved in costing, review and/ or auditing of funding mechanisms contained in State and Regional Plans.

Issue 3.6: Infrastructure costs and contributions rates are rising

Infrastructure costs are rising—particularly for land acquisition—as are contribution rates. Caps and thresholds introduced to encourage sector activity have, however undermined important market signals for development efficiency and are now likely to be reflected in higher land values.
The application of the essential works list can put councils' finances under pressure given their current inability to expand their rate base in line with population growth.

The caps are low and to request an IPART review or amended Ministerial Direction to exceed caps causes long delays in finalising contributions plans, which in turn, impacts funding and delivery of the required infrastructure. An IPART review may also not be a favourable option for councils as the essential works list is limited. The essential works list should be expanded to include construction costs for community facilities, particularly libraries. It is also considered reasonable to include costs to upgrade community facilities and open spaces. In dense established areas like Waverley, capital work to reprioritise roads to accommodate increased pedestrian demand and activation, by improving and increasing the public domain, should also be considered is essential. For example, Bondi Junction recently underwent large scale redevelopment with a significant increase in the residential population in this centre. Given the lack of public open space in and around Bondi Junction, a 'Complete Streets' project was developed to improve the public domain, recognising its importance as a 'third space' for local residents.

The uncapping of contributions in July 2020 has led to complaints from the development industry about this expense. However, while developer contributions per lot might increase by $40K in some places like the Blacktown LGA, this is driven by land acquisition costs being higher in this area. At the same time developer revenues have increased by $200K per lot in the last 10 years (since cap was introduced) while holding costs are also a fraction of what they were given much lower interest rates.

Issue 3.7: The maximum s7.12 rate is low but balanced with low need for nexus

Section 7.12 local infrastructure levies are low and do not reflect the cost of infrastructure.

Given that the rationale for these low rates reflects the lower nexus to infrastructure requirements, what issues might arise if the maximum percentages were to be increased?

Costs

If the 1% levy were to be increased it would be passed on to the landowner and marginally suppress land values. Landowners where the 7.12 levy applies would typically be in centres and have higher land values associated with higher connectivity from public infrastructure investment. As such, they are the recipient of the windfall gains accruing from this public spending and a marginally suppressed land price would be equitable and efficient.

A higher s7.12 levy would not impact development feasibility

Development feasibility is nebulous and changes regularly and rapidly. Feasibility testing was completed on a range of scenarios, including an increase of the s7.12 levy. This modelling demonstrates that an increase to the levy only has a negligible impact on development profit margin, especially compared to other factors that influence development margin. An increase from a 1% to a 3% levy would only change the profit margin by a maximum of 2 percentage points. Therefore, given such a negligible impact, it shouldn't form part of a consideration as a criteria.

Another key reason why higher contributions don't impact on development feasibility is because developers don't pay contributions, landowners do via lower prices. For example, before a developer purchases a site, they run a Residual Land Value feasibility assessment to calculate how much they should pay for the land. It is during this due diligence feasibility assessment that developers' 'price in' or account for the increase in contributions. An increase in the levy could also be phased in over time to allow developers to factor this cost into their feasibilities.

Benefits

The existing 1% levy does not have a strategic justification and was originally used in commercial and industrial areas, where a user pays s7.11 (94 at the time) could not be used as this is calculated on a per dwelling basis. It is not based on demand and was not based on any modelling of infrastructure requirements. The idea came from the City of Sydney, who had a similar levy in the City of Sydney Act 1988. The 1% levy became the de-facto option for employment areas and also dense inner city suburbs, where new development still obviously generated the need for additional infrastructure, but where it was too difficult to calculate nexus and apportionment for these dense inner city areas.

In inner city / infill areas, it is very difficult trying to draw a clear apportionment between development and infrastructure demand, which is why many inner city councils rely on the 7.12 contribution. The current 1% levy does not provide sufficient funds and it doesn't establish a link between increases in density and maintaining or improving liveability standards. Additional development can confer positive benefits such as critical mass to support greater provision of goods and services. However, additional development and increases in density also creates costs and negative externalities in the form of

congestion, visual impacts and overshadowing as well as greater contestability of public spaces and amenities.

While s7.12 has never been a clear 'user pays' funding mechanism, it has operated as a 'beneficiary pays' (of which user pays is a subset) mechanism. This recognises the beneficiaries of increased urban density should not just be the private interests who have been 'gifted' additional development rights (in the form of higher density zoning), but should also be the communities who experience the externalities associated with new development but don't see the trade-offs in terms of existing or improved infrastructure provision. What the community sees happening is land values increase due to rezoning but little return in terms of infrastructure investment. This is particularly acute in inner and middle ring Sydney where extra land for open space facilities is needed, but the land acquisition cost is prohibitively expensive. This has an impact on city performance and productivity when the political environment for locating more housing near jobs becomes difficult due to residents seeing no infrastructure or amenity improvements alongside densification.

The role of this beneficiary pays mechanism therefore transcends simply a user pays provision and creates a social contract for new development that may improve existing communities' acceptance of urban redevelopment. A higher 7.12 levy percentage provides an opportunity to not only mitigate the impacts of development, but to also create a net community benefit. It allows council to go beyond the bare minimum of infrastructure upgrades or maintenance. It can facilitate infrastructure development or upgrades that go beyond maintaining the status quo and which can actually improve infrastructure above baseline levels. It is to this extent, that development can be seen to be benefitting the public interest, particularly at a local level.

By linking increases in density to infrastructure improvements, a higher 7.12 levy not only ties increased demand generated by additional persons, but also links the planning externalities associated with additional development to improved or at least maintained levels of liveability. Hence a higher 7.12 levy creates a connection between increased development and liveability. The importance of this connection or nexus cannot be understated, particularly given the NSW Government's intentions to accommodate further growth in existing urban areas.

What would be a reasonable rate for s7.12 development consent levies?

A higher s7.12 levy improves liveability by funding public benefits that go above and beyond what Council is currently able to fund. To this extent, there is an argument that the 1% levy - being equivalent of slightly over $4,000 per dwelling - is insufficient to provide infrastructure to meet the needs of new residents. It is also unable to offset the negative impacts of new development with positive impacts from improved or upgraded local infrastructure provision. A higher levy of 3% should be the base level 7.12 contribution across all areas that use this levy and the levy shouldn't be arbitrarily capped at 3% either – increases should be based on merit, based on a final agreed set of criteria. As outlined elsewhere in this submission, the higher levy won't impact on development feasibility and would be passed on to the existing owners of higher density sites.

Given the above, Councils preference is that a higher levy should not be spatially limited to a strategic centre, local centre or economic corridor – but should apply to all areas. Notwithstanding, increases to the levy in these locations are supported in the absence of no increases.

Other issues

Given that the levy is based on construction costs, it is open to 'gaming' by the development industry who can have 'lowball' construction estimates to reduce their payable contributions. Councils should be encouraged to verify costs themselves for small to mid-size development (some Councils have a spreadsheet with a range of reasonable values) and should engage a QS for larger development. It is noted that some large Council's like the City of Sydney engages a QS for larger development, while Waverley Council does not currently do this.

Issue 3.8: Limited effectiveness of special infrastructure contributions

Special infrastructure contributions were introduced to strengthen delivery of state infrastructure. They can be an efficient and equitable mechanism for modest infrastructure cost recovery, while helping to ensure that development is serviced in a timely way. Over time, incremental changes and ad hoc decisions have, however, led to inconsistencies in their application, which may have limited their effectiveness.

Is it appropriate that special infrastructure contributions are used to permit out-of-sequence rezoning?

No, but if they are then they should full cost recovery to reduce the incentive of landowners to 'capture' planning process, particularly strategic planning, to have it deliver them a windfall.

Should special infrastructure contributions be applied more broadly to fund infrastructure?

Yes, but they should be based on value capture, such as betterment levy.

The SIC is broken and should be replaced with a betterment levy

A successful development industry lobby led to introduction of caps to s7.11 (formerly 94) in 2010 and also successfully lobbied to have the SIC reduced. The cost of the SIC is subsidised in the North West and South West Growth Areas by the NSW Government, with developers only having to pay 50% of the cost of state level enabling infrastructure. The cost of the SIC in Western Sydney is now 30% lower than when introduced in 2011.

In November 2007 the NSW Government foreshadowed a 'Rezoning Infrastructure Contribution' (also known as a 'Staged State contribution') to be paid either at the time of rezoning or at the time of sale. The approach recognised that contributions justified by uplift in land value must be levied at the time the uplift is realised, if the contribution is to be passed back to owner of the land. However, this approach was abandoned in the final package of reforms to developer contributions in NSW, due to "the existing market conditions"; again likely to be pressure from the developer lobby.

A more recent SIC is the St Leonards SIC, developed in 2019. A feasibility testing report indicated that the SIC would be structured to capture 50% of value uplift. Analysis demonstrated that those sites achieving the most residential uplift can afford to pay almost $60,000 per dwelling (see below

table. However, given that the SIC could only be a single rate, the feasibility testing report concluded that the "capacity of development to pay is examined by considering the SIC rate range most representative of sites able to tolerate to a SIC, i.e. occurrences within a bell curve. Using this approach, a SIC range of $21,000-$23,000 per dwelling results."

Notwithstanding the recommendation from the feasibility report, the end value SIC is $15,000 per dwelling, Therefore sites with minimal uplift will be hit with a higher burden than their '50% value sharing capacity to pay', while those sites with substantial uplift (the $60,000 per dwelling ones) only have to pay around one-quarter of their '50% value sharing capacity to pay'.

Proposed Planning Controls			SIC on Overall Dwellings	
Zone	Res. FSR	Non-Res. FSR	GFA	Unit
St Leonards Centre and Crows Nest Station				
B4	2:1	5:1	$250-$270	$21,000-$23,000
B4	3:1	1:1	No capacity to pay	
B4	5:1	1:1	$640-$660	$55,000-$57,000
B4	3.5:1	3:1	No capacity to pay	
B4	10:1	6:1	$440-$460	$38,000-$40,000
Crows Nest Village				
B4	2:1	2:1	$20-$75	$1,750-$2,250
B4	1:1	2:1	No capacity to pay	
St Leonards South				
R4	2.75:1- 4:1	-	No capacity to pay	

This is a clear case why a betterment levy needs to replace the SIC.

In the first instance, if a 'single rate' is required then the SIC could be expressed as a $/sqm rate (which was proposed in the Greater Parramatta Olympic Park area some time ago. It is equivalent to the net dollar amount of RLV of residential floorspace/sqm, so in this case would vary by precinct discounted by a suitable rate (50%, or preferably 25% like the ACT).

As outlined in our response to Issue 1.1 above, a standard percentage rate per dollar of betterment (value uplift) should apply across the state.

Should they be aligned to District Plans or other land use planning strategies?

Yes, land use and infrastructure funding alignment is critical.

Should the administration of special infrastructure contributions be coordinated by a central Government agency i.e. NSW Treasury?

Potentially. The DPIE has failed in their application of SICs and it may be that Treasury is less susceptible to policy capture from industry than DPIE, given their ability to 'cut through' industry messaging on contributions.

WAVERLEY COUNCIL

Issue 3.10: Affordable housing

Affordable housing contributions are made on top of other infrastructure contributions. The percentages are determined individually, and each scheme must demonstrate the rate does not impact development viability.

Is provision of affordable housing through the contributions system an effective part of the solution to the housing affordability issue? Is the recommended target of 5-10 per cent of new residential floorspace appropriate?

Yes, it should form part of a suite of mechanisms tackling the issue.

The NSW Government could use value capture to fund affordable housing, whereby any funds raised above the cost of infrastructure provision could be hypothecated to affordable housing. It would make sense from uplift in land values which price people, including key workers, out of inner city gentrified areas.

The market will not deliver affordable housing, so there is a need for intervention

Housing is desired to be more "affordable", but policies that actually lower home prices are too politically difficult and also come with macro-economic risks. So, the government often ends up doing 'busy work' to address the problem, while not focussing on achievable and scalable solutions such as large-scale social housing programs. This is the heart of the NSW and national housing dilemma that should be the focus of any housing strategy at any level of government. A realpolitik view is that this dilemma is behind the promotion of supply-focussed policy—it can plausibly be claimed to be helping reduce prices while in practice not having any price effects, keeping homeowners and investors happy and the construction sector ticking along. Given that market rate supply does not actively reducing market housing prices, then there is a clear case for intervention to deliver non-market housing, including affordable housing contributions. There is also an opportunity for Commonwealth tax incentives, including negative gearing and the capital gains tax discount, for investment housing to be reduced or removed.

The delivery of a large-scale intervention in housing supply would require significant public money. Interestingly, the government also gives away significant public money when it gives away additional property rights worth $8 billion a year.[6] Clawing back some of this windfall that Councils and the NSW Government confer to developers and landowners could go a long way to funding greater government intervention and deliver of housing. Such funding systems are usually known as value capture or betterment taxes, and the scope for funding far exceeds the current $900 million per year from infrastructure contributions across NSW. The NSW government should consider implementing a state-wide value capture levy to ensure consistency across NSW and avoid the current inconsistent application of Planning Agreements (based on value capture).

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[6] Koziol, M, 2020 'NSW missing out on $8 billion a year from failure to tax land-rezoning, inquiry told', Sydney Morning Herald,

The 5-10% target is too low and should be increased over time

Given the need for affordable housing in Sydney, the 5-10% target on uplift is too low and should be increased incrementally over time, to allow developers to factor in this cost in their feasibilities. This submission raises the fact that where a betterment levy raises funds surplus to providing infrastructure, then this could be hypothecated to affordable housing. The below breakout box provides an example of a best-practice affordable housing contribution based on a relatively like for like economic and social context for Sydney.

Affordable housing – London example

The UK and London have a longstanding system of affordable housing contributions. In 2017 with a new Mayor for London, the Greater London Authority (GLA) set affordable housing contribution benchmarks for London at 35% (with a long term vision to increase to 50%) of new development with 10 or more units. When the new mayor took office affordable housing contributions were as low as 13% of new developments.

Key points

- The affordable housing levy is set by each Council and can be higher than the GLA benchmark of 35%. For example some Councils have rates as high as 50%.
- Councils can also choose to apply the contributions to new developments with fewer than 10 dwellings.
- The affordable housing contributions are in perpetuity and the type and tenure of housing varies by each Council, based on the different needs. For example, the affordable housing contribution can be split between social housing, affordable rental (key worker), shared ownership (where you can purchase a portion, say 50%, of the house) and affordable purchase product (i.e. first home buyer), as well as different dwelling types: 1, 2 or 3-bed.

Viability assessment

- The 2010 Conservative Government introduced the 'viability assessment' in 2012 to stimulate the construction industry. An applicant can lodge a viability assessment with a DA to reduce their affordable housing contributions.
- The introduction of the viability assessment created a cottage industry of 'viability consultants' for developers to reduce or avoid affordable housing contributions. Therefore, the new Mayor of London (GLA) has tightened the ability for viability assessment to reduce contributions.
- If a new development provides the 35% GLA benchmark of affordable housing then it can proceed under 'fast-track', without providing a viability assessment, even if it is below a local Council's higher (e.g. 50%) benchmark.

Importantly, if an applicant wants to go below the AH benchmark for viability reasons (i.e. arguing they can only provide 20% affordable housing), and the GLA finds that the applicant can feasibly provide 40% viable housing, ***then the GLA will impose this higher contribution; even if above the 35% benchmark.***

Do affordable housing contributions impact the ability of the planning system to increase housing supply in general?

As argued above, housing supply is driven by market conditions and that changes in housing supply in Sydney have been driven by change to aggregate demand (influenced by investors including overseas, interest rates, macroprudential controls / access to credit, taxation settings, sentiment, etc.) not by any issues with supply costs such as restrictive planning controls, slow process, or high contributions. If affordable housing contributions were imposed overnight, then developers would absorb the costs. They wouldn't stop developing – that is led by the number of buyers. If known affordable housing contributions are known in advance, the development sector would pass this cost on to the landowner and reduce raw land values. Ultimately, the recent house price boom across Sydney has increased land values in the order of 50%. A marginally lower price for land as a result of affordable housing contributions would be an 'equitable' impost on existing landowners.

Issue 4.1: Sharing land value uplift

If investment in public infrastructure increases land values, then the benefits are largely captured by private property owners. 'Value capture' mechanisms can return a share of the value created by public investment to the taxpayer.
There are several ways a 'value capture' mechanism could be applied, including land tax, council rates, betterment levy, or an infrastructure contribution.

Where land values are lifted as a result of public investment, should taxpayers share in the benefits by broadening value capture mechanisms? What would be the best way to do this?

Yes, value capture mechanisms should be broadened to ensure that the private property owners who receive windfalls from public investment contribute a fair share. There is a need for greater equity in transport infrastructure spending.

The Committee for Sydney joins many other infrastructure experts in saying value capture has to be worked out early in the planning process. Under the heading "Capture first, announce later", the Committee warned in late 2015:

> *"It is important that governments have a regime in place before new transport routes are announced or new high density precincts are planned … Even a hint of a potential land use change in press release can increase the value of land in an area. If there is no value capture mechanism already in place much of this value creation can be lost. It can be politically hard to impose new levies retrospectively. It can also be economically distorting. All too often it becomes the "development" that gets levied, not the land. This is then passed on in the form of more expensive housing or if the levy is too onerous it can stop the development, and everyone loses. However, if a value capture mechanism is announced at the same time, or before, transport projects are identified, this sets the initial parameters for all – making the cost less distorting".*[7]

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[7] http://www.sydney.org.au/wp-content/uploads/2015/10/CfS-Issues-Paper-11-Are-we-there-yet-Value-capture-and-the-future-of-public-transport-in-Sydney-2015.pdf

Then in 2018 the Committee warned of not repeating past mistakes in failing to implement value capture:

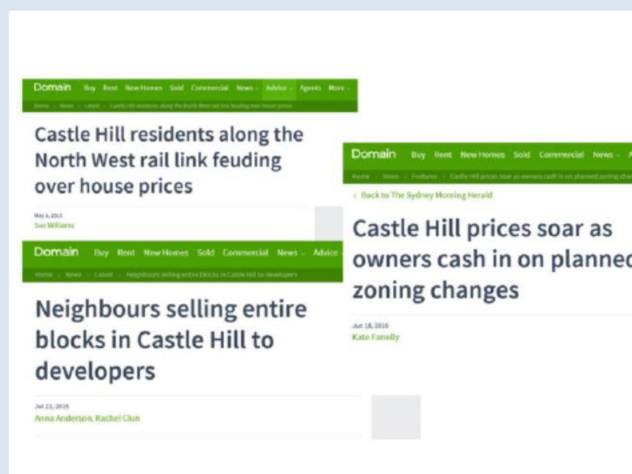
> It is widely accepted now … that a value capture approach should have been implemented in relation to the building of the North-West Rail Link (now Sydney Metro Northwest) as the costs of this massive project were carried by the public sector but the returns were privatised by land owners. We must avoid similar unearned private uplift to land values around the Western Sydney Airport arising from public intervention as rezoning there provides a real opportunity to introduce value capture with widespread public support. The same can be said of the Sydenham to Bankstown extension of the Metro: we must avoid history repeating itself and the government depriving the community of a significant and justified return.[8]

Along similar lines GLN Planning's Greg New produced a devastating analysis in late 2018 pointing out that land owners around the Badgerys Creek airport site have already made "huge" unearned gains on the back of the government infrastructure decisions and planning commitments. New asks the question: "Is it already too late for 'value capture' to help fund the high infrastructure costs in the Aerotropolis?".

While the above examples speak to large landowners profiting form windfalls, a value capture mechanism should equally apply to smaller lots including individual detached residential properties, as outlined in the below case study example from North West Sydney.

Value capture missed opportunity – North-West Sydney

With the proposed rezoning of detached housing sites to high density residential around new rail stations on the North West Rail Line. First the reports indicated the residents were feuding but then they organised and banded together to sell multiple lots to developers.



[8] https://www.sydney.edu.au/content/dam/corporate/documents/henry-halloran-trust/value-capture-on-urban-road-and-rail-projects-final-report.pdf

With the new rail stations being completed and rezonings in prospect house prices in Castle Hill rose dramatically. Three adjoining blocks close to the new Showground Station were sold for an estimated $40 million, with nine different developers vying for the site. Twenty freestanding houses straddling three streets in Castle Hill tripled in value to about $4 million each when sold in aggregate.

A related perversity of the increasing land values in the North West rail corridor is that the NSW state government is not only not getting a fair share of the uplift it has created but it is effectively paying twice for the rail line.

The value of the $8b rail line was capitalised into land values in the North West with the promise of enhanced accessibility and additional development potential –including in new release areas beyond Norwest and Bella Vista. However, to underwrite the supply of homes and limit the impact of development contributions for local infrastructure on house prices the government 'capped' s7.11 contributions at $30,000 per dwelling or residential lot in greenfield areas and $20,000 per dwelling or per residential. Where contributions exceed this under a legitimately prepared contributions plan the government contributed the difference under the Local Infrastructure Growth Scheme (LIGS) and The Housing Acceleration Fund (if sanctioned by IPART). But a significant component of the costs within a s7.11 contributions plan were based on land values for sites required for local drainage, road corridors, open space or community facilities.

The 2016/17 state budget the government announced a fourth tranche of funding for the housing acceleration fund and LIGS, with $537 million announced "to support local infrastructure and improvements to the planning system."

So as the land values rise from government's investment in infrastructure the government pays more to fund the difference between the s7.11 cap and the total amount. Rather than paying twice for infrastructure it would seem more sensible for the government to actually extract a return on the community's behalf via value capture mechanism for the value it is creating.[9]

Issue 4.2: Land values that consider a future infrastructure charge

When land is rezoned, there is often an increase in land values as a result of the change in development potential.

Should an "infrastructure development charge" be attached to the land title?

Yes.

Planning controls ration access to development rights (for the benefit and amenity of the community) and enables those who have access to them to gain the value of social infrastructure, amenity, the scarcity of access to city services and jobs, etc. The value uplift associated with changes to planning controls represents the value of the new property rights that allow for that development to take place, which are, until then 'owned' by the community. In other words, planning decisions are made in the public interest and the value of land is created by planning decisions (*ceteris paribus)*. Therefore, the

[9] NSW PIA Presidents Award Lecture – 'Putting the public interest back into planning', Festival of Urbanism, 02/08/2016.

value uplift that planning decisions generate is an unearned windfall gain to the developer granted by the public.

Given that value uplift is conceptually community property, the community have a legitimate claim to the benefits created by planning decisions. To this extent, value capture is not just a valuable funding mechanism, but a fundamental equity issue that places the public interest at the forefront of planning. The Planning Institute of Australia (PIA) position paper on Voluntary Planning Agreements also states that "VPAs are a powerful and effective tool to provide community benefits via 'value capture'" and that they "provide an opportunity for the community to share in part of the uplift in land value accruing to a developer from infrastructure investment, rezoning or development approval".

Value capture creates a nexus between density and liveability

In inner city / infill areas, it is very difficult trying to draw a clear apportionment between development and infrastructure demand, which is why many inner city councils rely on the 7.12 contribution. Section 7.12 does not provide sufficient funds and it doesn't establish a link between increases in density and maintaining or improving liveability standards. Additional development can confer positive benefits such as critical mass to support greater provision of goods and services. However, additional development and increases in density also creates costs and negative externalities in the form of congestion, visual impacts and overshadowing as well as greater contestability of public spaces and amenities.

At best, traditional 7.11 and 7.12 levies can only *mitigate* the negative externalities generated by additional development. The use of value capture in Planning Agreements provides an opportunity to not only mitigate the impacts of development, but to also create a net community benefit. It allows councils to go beyond the bare minimum of infrastructure upgrades or maintenance. It can facilitate infrastructure development or upgrades that go beyond maintaining the status quo and which can actually improve infrastructure above baseline levels. It is to this extent, that development can be seen to be benefitting the public interest, particularly at a local level and in the short to medium term.

By linking increases in density to infrastructure improvements, value capture not only ties increased demand generated by additional persons, but also links the planning externalities associated with additional development to improved or at least maintained levels of liveability. Hence value capture creates a connection between increased development and liveability. The importance of this connection or nexus cannot be understated, particularly given the NSW Government's intentions to accommodate further growth in existing urban areas.

The use of value capture in VPAs has allowed for Council to improve liveability by funding public benefits that go above and beyond what Council would have been able to fund just through 7.12 contributions. For example, two developments in the Bondi Beach area sought floor space ratio exceedances to incorporate additional apartments. Under Council's traditional 7.12 plan the developments would raise around $100,000, which would have limited benefits to the community. However, under two Planning Agreements Council raised close to $1.2 million. Despite the 'cost' to the developer they still pursued the VPA with Council as there was a substantial enough windfall gain

to create a win-win situation for both the developer (increased 'saleability' from an upgraded park next door) and local community. The DA was court approved and this money was used to fund an immediately adjacent park upgrade and public domain improvements and attracted significant community support (see Figures 1 and 2 below).

Figure 1 Concept plan showing location of VPA that funded the adjacent park upgrade.

Figure 2 Concept plan for park upgrade at Seven Ways, Bondi Beach

The use of value capture has also led to successes in affordable housing. Affordable housing facilitates the retention of diverse communities. Diverse communities are vital to the economic and social prosperity of our places. Value capture have been the primary source of funding for affordable housing in Waverley, accumulating $2.4 million for Waverley's Affordable Housing Program. This would not have been achieved through inadequate section 7.12 contributions plans.

Value capture does not imply conservative (low) planning controls

There has been some suggestion by the development industry that value capture creates an incentive for councils to keep planning controls low so that they can capture uplift in proponent led Planning Proposals.

Value capture does not keep planning controls low. The review and updating of planning controls is done regularly by local government through the preparation of comprehensive, multi-disciplinary studies that inform the Local Strategic Planning Statement, such as the Local Housing Strategy, and all Councils have housing and employment targets to meet. For example, in the Waverley LGA the bulk of development and Planning Agreements occur in Bondi Junction, whose development standards underwent significant review in 2013. This review was led by an external consultant and funded by the DPIE. The final development standards were a culmination of robust reviews from both a planning and urban design perspective (influenced by studies such as Bondi Junction Urban Design Review 2013, Bondi Junction Strategic Economic Overview 2004, and Bondi Junction Feasibility Report 2006). The community were involved throughout the preparation of the changes and are now comfortable with the certainty that the LEP provides.

Since these changes, there have been some circumstances where standards have been exceeded. Developers are welcome to provide evidence to support an exceedance but should not be the sole

beneficiary of any uplift in value on the site as it sits beyond what was previously accepted by the community, Council and the DPIE.

Value capture does not increase house prices

When announcing the 2016 amendments, Minister Stokes stated that "we have a case where assessment processes are being held to ransom, increasing costs for new homes by up to thousands – a cost being borne, in the end, by home buyers".

The argument that planning contributions increase house prices is commonly spouted by the development industry. However, this comment cannot by treated lightly as it has a profound influence in the way that Planning Agreements are viewed and, more seriously, how they need to be changed.

While this argument is compelling and intuitive, it is not borne out in the evidence and does not reflect the determinants of house prices. The price of dwellings is determined by the market – the balance of supply and demand. In other words, house prices are determined by how much the market is willing to bear. Additional development costs cannot be ‘passed on’ to the home buyer beyond the achievable market price for a dwelling. To assume that developers could pass on additional planning costs necessarily implies that developers are currently selling houses below their market price – an unlikely proposition.

The price of new dwellings will reflect the price of established dwellings, rather than the cost of development. In the short term, if a developer had not accounted for a cost (such as value capture), then these costs would be borne by the developer. In the medium to long term, the expectations of these costs would be built into the development cost profile before a site is purchased and would therefore reduce the price landowners could achieve for development sites (effectively shifting the windfall ‘planning gain’ from private to public interests). Hence value capture is not passed on to the consumer (end-buyer) but is reflected in lower land prices received by the landowner; which would still benefit from a windfall gain.

Value capture underpins strategic planning by lowering the economic payoffs from planning decisions

There is an argument that value capture incentivises Councils to rely on ‘spot rezonings’ to capture value from, rather than proactively updating zoning controls based on a strategic planning process. This argument is flawed for several reasons: firstly it assumes that developers didn’t exceed existing controls before value capture was introduced via VPAs (and wouldn’t exceed if value capture was ruled out); and secondly, it doesn’t understand that value capture reduces the incentive for developers to capture the system.

The ability to exceed planning controls existed before value capture was used in VPAs with Clause 4.6 of the Standard Instrument LEP and proponent led Planning Proposals. Before Clause 4.6 was introduced, SEPP 1 ‘Development Standards’ was used to exceed development standards in LEPs and was created shortly after the *Environmental Planning and Assessment Act 1979* (which itself introduced discretion compared to the *Local Government Act 1919*, which formerly governed planning in NSW). The ability to exceed existing planning controls is a long-established practice of the NSW

planning system and there is no evidence to suggest that value capture and planning agreements encourage ad hoc planning, including DA exceedances and spot rezonings. Ultimately, developers make these decisions – Councils don't ask developers to exceed their controls.

Value capture lowers the economic payoffs to private landowners from planning decisions. It reduces the incentive for developers to 'capture' the system in order to have it deliver them a windfall. In this way, value capture actually underpins a plan-led strategic system. By supporting strategic planning (land use and infrastructure coordination), value capture reduces the diversion of resources from identified growth areas (and hence limits what economists term 'coordination failure').

Discretion to vary planning controls is a longstanding feature of the NSW planning system. For example, six weeks after the Environmental Planning and Assessment Act 1979 commenced in 1980, SEPP 1 - Development Standards was introduced to allow variations to planning controls. In 2006, the Standard Instrument LEP was introduced and included cl 4.6 'Exceptions to development standards', which superseded SEPP 1. Removing value capture from VPAs won't stop developers seeking exceedance to existing controls – that would continue but with no shared value with the community.

Confidence in the planning system's focus on the public interest is at the core of upfront, evidence-based planning touted by the DPIE. A value capture policy relating to changes in zoning and development standards should be implemented statewide, outside of and additive to the development contributions system.

Value capture does not mean planning decisions can be bought

The Issues Paper and the draft Practice Note from DPIE indicates that value capture could lead to the perception that planning decisions can be bought and sold and that planning authorities may leverage their bargaining position based on their statutory powers. Some members of the community may express that a value capture VPA means you can buy an extra floor or two. This perception that Councils are simply 'selling floorspace' or 'selling decisions' is intuitive, but wrong and is not borne out in the evidence.

Value capture simply means Councils are putting a price on additional floorspace that would otherwise be given away for free. In fact, by having a clear value capture VPA policy which states upfront what the value capture contributions are creates transparency and certainty in the community that VPA decisions aren't being made 'behind closed doors'.

The assertion that planning decisions can be 'bought and sold' ignores the rigorous assessment that DAs and Planning Proposals with value capture VPAS must go through (including Cl4.6 statements and meeting the 'strategic' and 'site specific' merit criteria) to justify exceedances beyond controls. After they meet this process, all DAs and PPs (with VPAs) are generally assessed by the independent Waverley Local Planning Panel. More contentious or larger DAs and PPs are often determined by the Land and Environment Court and the NSW Government's Sydney Eastern City Planning Panel. Council does not determine DAs that have VPAs associated with them. Also, Council only considers Planning Agreements for endorsement after the DA has been approved. These elements ensure that there is no

potential political or officer interference in the assessment of Planning Agreements. The take home is that applications cannot be approved unless they go through a rigorous and independent assessment process.

Value capture is not simply a 'cash grab'

There is concern that value capture is simply a 'cash grab', especially where it is expressed as a % on uplift or in $/sqm terms. The broader issue is that there are concerns the value uplift is not linked to Capital Works Programs, would and may go into consolidated revenue and not fund works related (or nearby) to the development.

The issue of substance here isn't related to value capture. The issue is that VPAs should be linked to contributions plans and Capital Works Program or demonstrate that works benefit residents of the new development. For example, Waverley's PA Policy highlights upfront that VPAs negotiated in Bondi Junction should fund the *Complete Streets* program, which is a large-scale public domain upgrade to improve the liveability of this centre.

Council has to balance any additional planning harm – in terms of bulk, scale, height, overshadowing, overlooking, loss of privacy – which generally occurs immediately surrounding the site against contributions that fund community infrastructure not necessarily directly adjacent to the site (or in the form of affordable housing). Council actively seeks to provide the funds to nearby open space (and in Bondi Junction towards the *Complete Streets* program), which provide a very good nexus between increases in density and liveability.