Urban Development Institute of Australia
NEW SOUTH WALES

Review of Development Levies

Submission of the Urban Development Institute of Australia

November 2008

NSW Government Review
Development Levies

Executive Summary

The widespread expansion of development levies to fund local and state infrastructure has played a significant role in constraining dwelling production in New South Wales (NSW) and in Sydney in particular. The application of charges at local, state, and federal level have combined with inefficient regulatory and approval processes and a lack of commitment to long term strategic priorities to compromise development feasibilities and constrain the industry's capacity to deliver new housing at prices within the market's capacity to pay. This has been evidenced by sustained record low levels of dwelling production and massive reductions stamp duty revenue for the NSW Government.

It is important to emphasise that while there are some cyclical elements exacerbating the current downturn in the NSW property market, there are significant structural problems that have existed well before the recent constriction of credit markets. These structural problems will continue to constrain the future recovery of the market if they are not addressed as a matter of absolute priority for the Government. In turn, this will continue to undermine the NSW Government's economic growth framework and its housing targets as reflected in the Metropolitan and Regional Strategies.

UDIA NSW seeks to emphasise that this review must be the first step in a process of comprehensive reform to the property levy and tax structure in NSW. While there are certainly immediate actions that must be taken to provide stimulus for dwelling production, there are underlying constraints to the competitiveness of the regulatory and economic framework for urban development in this state that should be considered as part of a broader review. These include the dependence of the Government on cyclical stamp duty revenue, the timing and application of GST on the development process, and expansion of land tax during a period of prolonged downturn in the property market.

In framing its response to this review, UDIA NSW has put forward a balanced perspective on the legitimate role of levies in regard to the staging and efficiency of infrastructure provision and recognises the need for an element of cost sharing in the development process. UDIA NSW has identified the potential for significant reductions in the application of levies in the special infrastructure contribution (SIC), local development contributions, and utility levies.

UDIA NSW contends that the use of the SIC and local development contributions must be rationalised to reflect only the baseline infrastructure needed to deliver housing to new release and infill areas. Both of these contribution frameworks have been burdened by capital items that are in excess of what the market has the capacity to fund and are items that should be funded through broader, more efficient revenue sources. The immediate rationalisation of the scope of the SIC will deliver a $10,000 saving to the production of housing in the Sydney Growth Centres and a UDIA NSW review of five existing Section 94 Plans across NSW to deliver only baseline infrastructure identified reductions of between 29% and 68% of the charges currently being levied on new housing.

UDIA NSW has taken the opportunity to propose structural reform to the application of water and sewer infrastructure charges levied by the water utilities that will be at no net cost to Government yet will save new homebuyers on the fringe up to $12,000 per lot. The application of a broad, simple, efficient annualised charge across a water utility's entire catchment would in the example of Sydney Water Corporation be less than $40 per connection and would reverse the geographical and intergenerational inequities that the current structure yields.

UDIA NSW contends that this review must recognise that the use of narrow, upfront charges has made the greatest contribution to the current housing affordability problem in NSW. Their continued role in financing and delivery of infrastructure to support the development process must be reformed to reflect more equitable and efficient cost sharing if NSW is to recover from its current uncompetitive positioning. Without sustainable, systemic reform to the development levy structure, this state will continue to produce less houses than it was fifty years ago and see investment in new housing directed to other states.

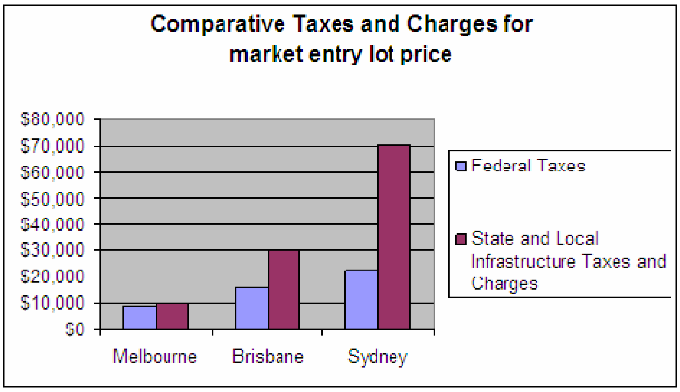
INTRODUCTION

UDIA NSW is a proud advocate of the urban development industry and its customers, the people of NSW. We represent over 500 organisations and our members include developers, regulators, and affiliated professionals. Our advocacy efforts are directed towards three major issues:

- housing affordability;
- investment certainty; and
- sustainability.

As responsible and ethical contributors to the public debate, UDIA NSW has taken the opportunity to review the development levy structure in NSW and provide recommendations that it believes should be adopted to assist in the recovery and long term viability of the urban development sector.

The application of state and local development levies and charges has irrefutably contributed to consecutive years of historic declines in dwelling production in NSW. Without widespread reform to the levy cost structure for new development, the urban development industry will remain significantly depressed with major implications for housing affordability and economic growth in NSW.



There has been recognition from the NSW Government that its policy settings for the financing and delivery of infrastructure to support new urban development have resulted in a cost structure for new development that does not equal the market's capacity to pay. A comparison of the cost structure between Sydney and competing major centres provides a particularly alarming illustration of how uncompetitive the environment for housing production has become. The graph left of page shows that new homebuyers in Western Sydney pay on average seven times more in state and local levies than in Melbourne, and twice as much in Brisbane. Sydney is clearly not competitive.

The NSW Government has now committed to reviewing the development levy structure for greenfield, infill and employment lands, focusing on development levies applied by the state government, local government, and infrastructure utilities. UDIA NSW supports this approach to the review as it is not just one levy in isolation that is responsible for the structural constraints to the industry, but the quantum of the combination of the charges, combined with a costly and inefficient regulatory and delivery process. UDIA NSW understands that the Review will be undertaken on the basis of three underlying principles:

1. the beneficiaries of rezoning and infrastructure provision should contribute to the cost of its provision;

2. the Government will not accept arguments about why there should be no levies; and

3. the development levy structure must be sufficiently robust to withstand the property cycle.

In preparing its submission to the NSW Government on its review of levies, UDIA NSW has consulted extensively with its members and in particular its major corporate members who represent most of the urban development industry's leading participants. UDIA NSW has provided a suite of recommendations it believes, if adopted, will provide stimulus for activity in the residential sector, and will provide the framework for a more sustainable and equitable cost structure for development in NSW.

Special Infrastructure Contributions

Previous revisions to the quantum of the special infrastructure contribution (SIC) in the Sydney Growth Centres have failed to yield any significant stimulatory impacts on the feasibility of development in the release areas. Regardless of the reductions in the charge, the quantum still reflects a significant disparity between the cost structure of new development in Sydney, compared with other competing centres. The special infrastructure contribution remains a significant impediment to the delivery of new housing in Sydney.

The special infrastructure contribution does provide some benefit to the urban development industry and the wider community by identifying and costing the future infrastructure needs of both sectors in the growth centres. UDIA NSW has consistently provided in-principle support for this approach.

UDIA NSW contends that the principal benefit in the utilisation of the special infrastructure contribution framework is the flexibility it provides for developers to deliver the identified major capital works to support a new release area and receive credit for this investment against any future levy obligation. Many developers are experienced in delivering major capital investment and have the expertise necessary to respond to market demand in an efficient manner. In the absence of clear timeframe commitments from the government, at least the developer is able to deliver infrastructure when it is needed. The SIC framework also enables a lead developer to take the initiative and deliver key lead-in infrastructure where no other stakeholder is willing to do so, be it other landowners or the government. UDIA NSW therefore supports the use of the special contributions framework for delivering major capital works on the basis that the framework remains transparent.

In practice the special infrastructure contribution framework remains a constraint to the affordable delivery of housing because it is burdened by capital items that are in excess of what the market has the capacity to fund. UDIA NSW contends that by rationalising the scope of the special contributions framework to deliver only core baseline infrastructure that actually facilitates and stimulates development, **the NSW Government could dramatically reduce the SIC by more than forty per cent (40%).**

SIC Levy Calculator (Based on GCC Model)				
Infrastructure	**100% Attributable**	**100%Reduced List**	**75% Attributable**	**75%Reduced List**
Roads	$2,857,464,000	$2,857,464,000	$2,143,098,000	$2,143,098,000
Rail	$1,135,373,000	$162,923,000	$851,529,750	$122,192,250
Bus	$340,896,000	$340,896,000	$255,672,000	$255,672,000
Emergency	$7,022,000	$0	$5,266,500	$0
Health	$18,942,000	$0	$14,206,500	$0
Education	$394,485,000	$0	$295,863,750	$0
Open Space	$653,234,000	$0	$489,925,500	$0
Planning and Delivery	$440,778,000	$51,663,000	$330,583,500	$38,747,250
Total	**$5,848,194,000**	**$3,412,946,000**	**$4,386,145,500**	**$2,559,709,500**
Estimated NDA	12317	12317	12317	12317
Allow 7% undeveloped	11455	11455	11455	11455
Employment Land	2574	2574	2574	2574
Equivalent NDA (employment)	1107	1107	1107	1107
Equiv NDA	12562	12562	12562	12562
Levy per NDA	$465,560	$271,696	$349,170	$203,772
Levy per dwelling	**$31,037**	**$18,113**	**$23,278**	**$13,585**
Reduction in levy	-	42%	-	42%
Employment land is 43% of residential levy				
Assumes 5% of NDA will never be developed and 2% to riparian and environmental.				
Reduced List removes SW Rail Link, Richmond Line Duplication, open space, GCC costs.				

RECOMMENDATION 1

UDIA NSW recommends that the application of the special infrastructure contribution be limited to essential baseline infrastructure required to support the development of a release area.

RECOMMENDATION 2

UDIA NSW recommends that the NSW Government exclude regional NSW from the expansion of the special infrastructure contribution in recognition of the failure of the current framework and the significantly lower retail price points for housing and employment creation in these areas.

There are infrastructure items that have and will in the future be identified that will be fundamental to ensuring the development of the release area adequately supports the needs of the community. These may include the land required to support education and health facilities, as has been the case in the growth centres and it is important that these items are provided for through a revenue source that better reflects the intergenerational benefits they provide. This revenue source must be alternative to upfront development levies.

UDIA NSW suggests that the Government consider the use of special rate provisions for new release areas that spread the prescribed cost of public capital expenditure over a significantly greater period of time. This method of contribution is considerably more efficient and shares the cost amongst a greater proportion of beneficiaries to the original decision to rezone and provide infrastructure for the release area. Use of this approach should not however diminish the NSW Government's contribution to key infrastructure. The overall model should be one where up front developer charges are reduced, with some costs transferred to a special rate framework to better address intergenerational equity issues, while still ensuring a strong contribution from the NSW Government in recognition of the wider responsibilities of Government to facilitate affordable housing and socially sustainable communities.

RECOMMENDATION 3

UDIA NSW recommends that the cost of delivering major infrastructure that is outside the scope of baseline requirements to deliver housing but is still fundamental to supporting the new population be funded through alternative revenue frameworks which spread the cost to residents over time.

The timing of the SIC payment also has major implications for the investment risk associated with development and also with the capacity of developers to meet market demands for housing in an efficient and cost effective manner. The payment of the special infrastructure contribution at the linen plan stage exposes developers to significant financial pressure from holding costs at a time while other options are available that would significantly reduce cash flow implications for development and better align with demand for services.

UDIA NSW recommends that the payment of the special infrastructure contribution be deferred until settlement of sale. This will provide greater investment certainty for development and will also minimise the cost of the levy to future homebuyers by limiting the project's exposure to interest payments while the marketing/sales process is undertaken.

RECOMMENDATION 4

UDIA NSW recommends that the payment of the special infrastructure contribution be deferred until settlement of sale of the individual lots – as currently occurs with the payment of stamp duty.

Local Development Contributions

The local contribution framework has played an important role in the delivery of baseline infrastructure facilities to support new development – particularly where developers have been able to deliver infrastructure as in-kind agreements to credit against payment of levies or in fragmented areas where no single developer can afford to provide such infrastructure. The expansion of contributions plans to fund more advanced facilities has been reflected in a significant increase in the quantum of charges and significant disparities between contributions plans in different LGAs.

Recent reforms to the local levy contribution framework through the Government's planning reforms will likely result in a relatively minor rationalisation of the scope of facilities that can be included in plans and will not necessarily lead to lower levies for new development. There are structural and procedural inefficiencies that prevent councils from making best use of development contributions and this has resulted in the accumulation of unspent levies. These include:

1. the spatial and temporal base for development contributions is often too narrow to allow for efficient revenue collection and can result in delayed and fragmented capital expenditure;

2. the scope of facilities included in contributions plans can be too broad, with only a proportion of the cost of each capital item apportioned to the revenue from development contributions. This means that councils are required to fund the remaining capital cost from existing consolidated holdings or other revenue streams; and

3. there are no third party review mechanisms to confirm that councils are making prudent assessments of infrastructure demands and ensuring efficient procedures and structures for delivering the infrastructure in a timely fashion. There are also no review mechanisms that can compel councils to spend accumulated funds.

Despite the structural problems with the local government levy framework, the principal constraint to the delivery of new housing is the quantum of the charges that are being applied. UDIA NSW contends that the most simple, equitable and effective approach to addressing this issue is to restrict the quantum of the levy charged to new homebuyers to just the baseline infrastructure required to facilitate development and allow councils to utilise alternative revenue sources to fund additional community facilities.

UDIA NSW recommends that baseline infrastructure from which a charge could be levied to new homebuyers should be explicitly limited the following items:

- local roads;
- local bus facilities;
- local parks;
- local car parking facilities; and
- drainage and stormwater management works.

Any further items, being those codified as community infrastructure in the recent planning reforms should be funded from alternative revenue sources. UDIA NSW recommends that an alternative source for funding these additional items may include the use of a differential rate for the development of a release area that is applied over a prescribed period to either recover the costs of specific infrastructure provision or fund the investment in future, identified and costed works. Where these facilities benefit the population beyond a release area, the rate should be applied to that population area.

Alternatively, UDIA NSW has advocated previously for the replacement of rate pegging with a structured differential rating scheme for whole LGAs in recognition of the different roles that councils have to play in delivering broader regional outcomes. This scheme would provide a greater degree of flexibility to account for councils who must provide for significant increases in dwelling production or employment while maintaining a regulatory role for the NSW Government or its delegate, such as IPART.

In replacing the current rate pegging structure, UDIA NSW suggests that IPART would have a role in providing a framework for local government rates through:

- determining a series of differential rate variations for groups and/or types of councils based on an assessment of the need for the LGA to achieve local and sub-regional outcomes such as employment and housing creation;

- providing advice to councils on appropriate rate ranges and processes; and

- reserving the right to cap proposed council rate increases if IPART determines the increase to be unjustifiable or unreasonable.

One of the distinct benefits of making councils use broader based charges applied over a longer period of time to deliver community infrastructure is that the council is accountable to the rate paying community to actually deliver the infrastructure in a timely manner. It also provides a far greater role for rate payers in providing input into determining what infrastructure and facilities should be provided for the community.

UDIA NSW has reviewed a number of contemporary contributions plans in both Metropolitan Sydney and Regional NSW to determine the reduction in the quantum of charges being applied if the Institute's recommendation on restricting local levies to baseline infrastructure. The table below demonstrates the current charge being applied, the potential future charge, and the percentage of the charge that would be saved by introducing a more rationalised and equitable policy.

Release Area LGA	Estimated dwellings	Current Contribution per lot	Revised contribution per lot	Percentage reduction in contribution	Some of the facilities omitted from revised plan
Warriewood Valley Pittwater Council	1886	$74,820	$39,639	47%	Library services, community facilities.
Northlakes Release Area Lake Macquarie	4249	$19,130	$13,619	29%	Community vehicle, library, three multi purpose centres
Moonee Release Area Coffs Harbour	1686	$14,954	$9,659	35%	Community centre, district open space

RECOMMENDATION 5

UDIA NSW recommends that the local government contribution levied on new homebuyers be rationalised to only include items that are essential to the delivery of new housing and employment. These must be limited to:

- *local roads;*
- *local bus facilities;*
- *local parks;*
- *local car parking facilities; and*
- *drainage and stormwater management works.*

Similar to the application of state levies, the timing of payment of local contributions can have a significant influence on the efficiency of development, and therefore the delivery and cost of new housing. In many cases major developers will prefer to undertake the majority of the key lead-in infrastructure works themselves in return for credit against levy payments so that they can have greater influence over the timing and indeed the efficiency of the development process.

In some cases there are infrastructure items, such as those between or across fragmented holdings that are better delivered by the local council. In this event, many developers have experienced the not-uncommon practice of paying contributions but waiting a long time for the council to deliver the required infrastructure. The revelation by the former Minister Planning in February 2008 that NSW Councils had collectively accumulated $1.3 billion in unspent s94 contributions is testament to this problem.

UDIA NSW recommends that the payment of local development contributions be deferred until settlement of sale. This ensures that developers reduce borrowing and improve cash flow to allow further development.

RECOMMENDATION 6

UDIA NSW recommends that the payment of the local development contribution be deferred until settlement of sale of the individual lots.

Utility Levies

The current water and sewer levy framework is inherently complex, geographically inequitable, and very costly to administer. The current model relies on the release of new land to fund the provision of water, sewer and water recycling infrastructure on the urban fringe and the renewal of infrastructure in existing urban areas. The significant disparity in DSP charges across the Sydney catchment in particular reflect the considerable geographical inequities that the current framework provides.

The low, and in many cases non existent charges account for Sydney's eastern affluent suburbs and reflect the presence of existing infrastructure where the capital cost for such services has been discharged. The initial investment in those pipes and pumps was paid by the NSW Government from consolidated revenue. This is in contrast to those looking to buy in financially constrained Western Sydney and Illawarra where price signals have been established to recoup the investment on such infrastructure.

Accordingly, new homebuyers in the eastern suburbs of Sydney benefit from the investment and foresight of previous generations while new homebuyers in Western Sydney pay the full cost, upfront for infrastructure for themselves and future generations. The current methodology requires an average connection cost per lot in Western Sydney of $15,000 per lot when combined with upfront costs for recycled water.

UDIA NSW contends that an alternative approach to funding infrastructure must be implemented that provides a recurrent revenue stream for the water agencies that is not dependent on the release of new land to recover capital investment in water and sewer. The applications on an increase to the annual charges across all ETs within a catchment to fund new infrastructure provision is an equitable and sustainable financial model that will assist with affordability for new homebuyers. The following framework illustrates how the model will work:

1. fund the connection to water and sewer infrastructure as a forward investment to increase the numbers of ETs;

2. increase the annual charge across all ETs – UDIA NSW understands that in the case of the Sydney Water Corporation catchment, this would be a net $20 per annum increase;

3. allows investment in urban renewal areas;

4. gives relief to new homebuyers in greenfield areas;

5. produces recurrent revenue for the water utility beyond 25 years – as would indicatively be the case in the Sydney Growth Centres under the current framework; and

6. creates an incentive for water agencies to deliver infrastructure in a timely manner.

The application of an increase to the annual charges on a catchment-wide basis to fund new infrastructure provision is an efficient and equitable method of infrastructure financing that is critical to the delivery of new housing. UDIA NSW understands that Sydney Water Corporation have provided in-principle support for this or a similar model. While this model above is fundamentally based on the Sydney Water Corporation catchment, the methodology would apply to regional areas on a similar scale with some capital grant support from the Commonwealth or State Government.

This approach would bring relief to homebuyers in new release areas in Sydney of an average of around $15,000 per lot. This approach will result in no net cost to Government and will generate efficiencies in the unnecessarily burdened administrative functions of the utilities charged with managing the current framework.

UDIA NSW contends that this methodology must also apply to the provision and funding of recycled water infrastructure in Western Sydney. The current levy framework for recycled water demands a payment by new homebuyers to fund its provision – this is despite the fact that the same homebuyers are contributing to the funding for the development of the desalination plant through increased annual charges. This is highly inequitable.

The success of the broad, annualised charge approach in delivering water and sewer infrastructure to new development will be dependent water utilities having a transparent and coordinated infrastructure delivery program. This would be based on the Metropolitan Development Program (MDP) which must be publicly released and would ensure that developers are informed of the utilities investment commitments and priorities, and not second guessing an infrastructure program that has not been made public.

This process underscores the importance of transparency and consultation in the Government's preparation of the MDP. The last public release of MDP contains dwelling production figures for 2005. In this regard the NSW Government is compromising investment certainty and the lack of consultation with the development industry is negatively impacting the validity of the figures the Government is purportedly using to inform public capital investment. Greater consultation with the industry will ensure that the Government and utility providers have greater awareness of developers' investment priorities and can therefore provide infrastructure in a more efficient and timely fashion.

Once the industry is aware of the water utility's priorities and have certainty over delivery timeframes, developers can have the option of developing ahead of sequence and pay the water and sewer costs upfront. These costs would then be repaid by the utility once the planned infrastructure delivery reached the accelerated development precinct. This framework has worked very successfully in the past and is considerably more cost effective for both the infrastructure provider and the end user, the homebuyer.

RECOMMENDATION 7

UDIA NSW recommends that the water, sewer and water recycling infrastructure be funded through increased annual charges collected across every connection within the water utility's catchment.

RECOMMENDATION 8

UDIA NSW recommends that that Government commit to the comprehensive production and annual release of the Metropolitan Development Program for Sydney and major regional centres to inform public capital expenditure and guide investment in urban development.

Conclusion and Recommendations

The Government must act swiftly and decisively in reforming the levy structure for urban development in NSW. This state cannot afford another year of record low dwelling production and without dramatic intervention in the financing and delivery of infrastructure to support new urban development, NSW will continue to significantly undersupply the demand for new housing and the impacts on housing affordability will continue to escalate.

In consultation with its members, some of the leading industry participants in NSW, UDIA NSW has developed a range of alternatives to the current levy and delivery framework for infrastructure that it believes, if implemented, would significantly assist in stimulating development activity and improve housing affordability in NSW. By focusing development levies on essential baseline infrastructure and apportioning the cost of delivering major community-wide infrastructure with a broader base of beneficiaries to that investment, the Government can significantly reduce the some of the major cost impediments to home ownership in NSW and Sydney in particular.

UDIA NSW has estimated that its recommendations if implemented appropriately will deliver a minimum average reduction in levies of at least $30,000 per new dwelling in Western Sydney. This will stimulate demand in new housing and provide opportunities for developers to bring supply to the market while meeting the Government principles for cost sharing of infrastructure provision.

UDIA NSW offers the following recommendations for the review of development levies:

1 UDIA NSW recommends that the application of the special infrastructure contribution be limited to essential baseline infrastructure required to support the development of a release area.

2 UDIA NSW recommends that the NSW Government exclude regional NSW from the expansion of the special infrastructure contribution in recognition of the failure of the current framework and the significantly lower retail price points for housing and employment creation in these areas.

3. UDIA NSW recommends that the cost of delivering major infrastructure that is outside the scope of baseline requirements to deliver housing but is still fundamental to supporting the new population be funded through alternative revenue frameworks which spread the cost to residents over time.

4 UDIA NSW recommends that the payment of the special infrastructure contribution be deferred until settlement of sale of the individual lots – as currently occurs with the payment of stamp duty.

5. UDIA NSW recommends that the local government contribution levied on new homebuyers be rationalised to only include items that are essential to the delivery of new housing and employment. These must be limited to:

   - local roads;
   - local bus facilities;
   - local parks;
   - local car parking facilities; and
   - drainage and stormwater management works.

6. UDIA NSW recommends that the payment of the local development contribution be deferred until settlement of sale of the individual lots.

7. UDIA NSW recommends that the water, sewer and water recycling infrastructure be funded through increased annual charges collected across every connection within the water utility's catchment.

8. UDIA NSW recommends that that Government commit to the comprehensive production and annual release of the Metropolitan Development Program for Sydney and major regional centres to inform public capital expenditure and guide investment in urban development.