Chapter 6

The impact of state and local taxes, fees and charges on housing affordability

6.1 According to many witnesses, the taxes and fees that apply to housing transactions and construction add significantly to housing costs. While Commonwealth taxation settings are often regarded as adding to housing demand (and, in a market with supply constraints, housing costs), state and local taxes were identified by witnesses as adding directly to the supply-side costs of housing.

6.2 This chapter considers the effect of state and local taxes on housing affordability, including state stamp duties on conveyances (referred to henceforth simply as 'stamp duties'). The overwhelming weight of evidence received by this committee suggested stamp duties are a highly inefficient and inequitable means of taxing land and improvements, and also undermine home purchase affordability. Flawed as stamp duties might be as a form of taxation, states and territories remain heavily reliant on the revenue they provide. Acknowledging this, some witnesses noted that any removal or reform of stamp duties would likely require a shift to a different revenue source. Attention in this respect generally settled on a possible broadening of land taxation, including its extension to owner-occupied property. The committee also heard arguments in support of broad-based land taxation on the grounds that its application would help discourage excessive speculation and overinvestment by investors and owner-occupiers.

6.3 This chapter also considers whether infrastructure fees and charges levied by state and local governments, most commonly in relation to greenfield housing developments, undermine housing affordability. In doing so, this chapter also outlines and addresses concerns expressed by some witnesses regarding the apparent lack of transparency and equity in the application of infrastructure fees and charges.

The burden of state and local taxes, fees and charges on new housing stock

6.4 Some submitters highlighted the costs that taxes and fees added to new housing construction, and the extent to which these costs were ultimately reflected in higher house prices. The taxes and fees referred to in this respect included some Commonwealth taxes, notably the Goods and Services Tax (GST). However, on the whole witnesses focused on state and local taxes, fees and charges.

6.5 Although not referring exclusively to state and local taxes, the HIA told the committee that in 'absolute terms, new housing is the second most heavily taxed sector in the Australian economy', out of a total 111 sectors. The HIA argued that any national tax reform agenda should consider how to reduce this tax burden.[1]

6.6 Similarly, the UDIA emphasised the relatively high tax burden on new housing and its impact on housing affordability:

> A major contributor to the high cost of housing in Australia, and subsequently affordability pressures in recent years is the escalating level of taxes and charges on new homes. The development and construction industry is one of the most heavily taxed sectors in the Australian economy, with various government taxes and charges accounting for up to 44% of the price of a new house in some cities. Many of these taxes are economically inefficient and inequitable, further discouraging investment, contributing to Australia's housing shortage, and worsening housing affordability.[2]

6.7 The UDIA continued that while a large proportion of this tax was levied by state and local governments:

> …their replacement with more equitable and efficient taxes will only be achieved with cooperation and leadership from the Commonwealth, due to the vertical fiscal imbalance experienced between Australian Governments.[3]

6.8 JELD-WEN provided more detail on the cost taxes and fees added to new housing. Citing research by the Centre for International Economics, JELD-WEN indicated that:

> More than 35 per cent or in excess of $100,000 of the cost of a new house and land package in the eastern state capital cities, consists of the GST, development charges, stamp duty, land tax, building fees and charges; in many cases, these indirect taxes and charges cascade throughout the acquisition and development pipeline to final sale.[4]

Stamp duty

6.9 While each state and territory levies stamp duty on the transfer of property on a progressive rate scale, rates and thresholds vary from jurisdiction to jurisdiction. As the final report of the Henry Review noted, the average rate of stamp duty across the states rose from 2.45 per cent in 1993 to 3.25 per cent in 2005, 'largely due to the non-indexation of the scales in the face of property appreciation'. The highest rate of stamp duty, the Henry Review further noted, was 7 per cent for residential properties valued above $3 million in New South Wales.[5] Stamp duty revenues are volatile, because

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1 Dr Harley Dale, Chief Economist, Housing Industry Association, *Proof Committee Hansard*, 30 July 2014, p. 43; Housing Industry Association, *Submission 178*, pp. 6–7.

2 Urban Development Institute of Australia, *Submission 190*, pp. 11–12.

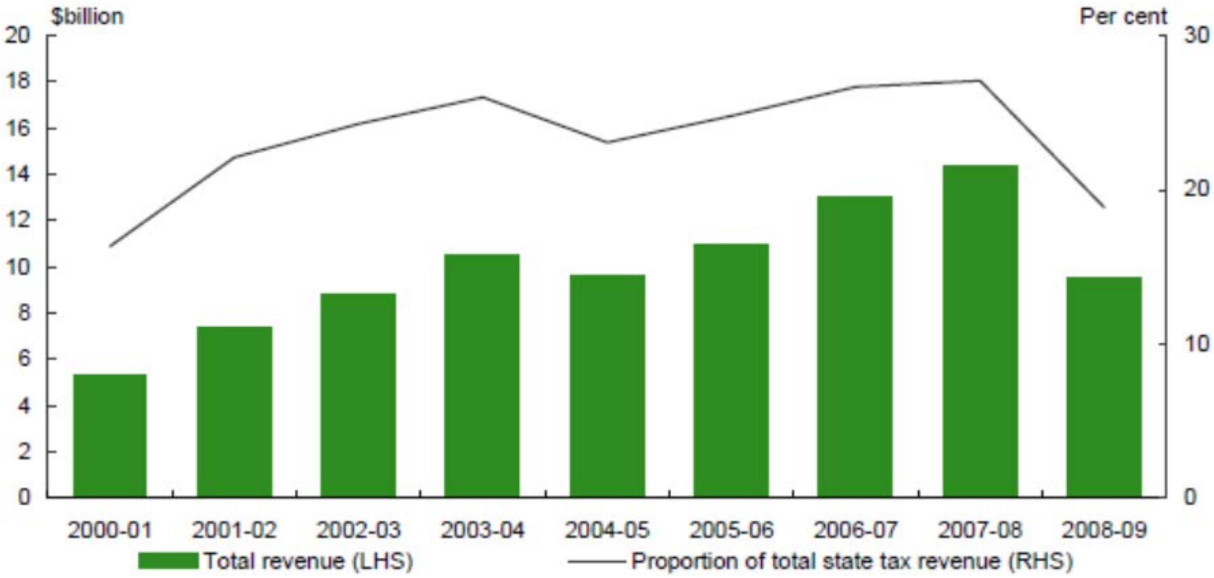
3 Urban Development Institute of Australia, *Submission 190*, pp. 11–12.

4 JELD-WEN Australia, *Submission 54*, p. 7.

5 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), pp. 251–52.

they are determined by the value and volume of properties being transferred. While volatile, these revenues consistently make up a very substantial proportion of the revenue raised by states and territories. For instance, in 2007–08, stamp duties raised $14.4 billion for the states and territories, more than 25 per cent of total state tax revenue that year (see Figure 6.1 below). In some states, stamp duties have at times been the single largest source of revenue.[6]

Figure 6.1: Revenue from conveyance duty



Source: Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), p. 254.

6.10 While acknowledging the reliance of states and territories on stamp duty revenue, many witnesses were critical of the effect stamp duties had on housing affordability and economic productivity. The REIA, for example, argued that stamp duties:

> …represent additional costs to property transactions, thereby discouraging turnover of housing and distorting choices between renting and buying, and between moving house and renovating. Individuals who move more frequently would pay more taxes than those who move less. Others, who would have to buy or sell if they changed jobs, could be deterred by these costs thus reducing labour mobility. These distortions lead to…sub optimal

6 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), pp. 253–54.

> outcomes, reduce investment in the property market and impede labour mobility.[7]

6.11 The Residential Development Council (part of the Property Council of Australia) also argued for the abolition of stamp duties. It noted the various inefficiencies and distortions created by stamp duties, including distorting the decisions people made about where to live.[8]

6.12 Like the REIA, a number of submissions highlighted not only the costs stamp duty imposed on the purchase of housing, but also the negative impact on labour mobility and productivity more broadly. For instance, in her submission, Associate Professor Yates suggested that stamp duty 'can discourage turnover, influence housing decisions and inhibit mobility'.[9] Similarly, AHURI referred to the 'disincentive to residential mobility for existing home owners wishing to sell and purchase another property especially in higher valued areas'.[10] The UDIA explained that stamp duties:

> …distort the efficient allocation of housing and land by penalising owners for moving to properties that best suit their needs. This has the effect of damaging economic productivity by constraining labour mobility, as the Productivity Commission recently reaffirmed in its study on Geographic Labour Mobility.[11]

6.13 Mr John Hawkins also highlighted how stamp duties can distort decision making in a way that negatively impacts on housing affordability:

> The relevance for housing affordability is that by discouraging people from moving houses, it tends to lead to people remaining in houses that do not suit them. For example, an older couple whose children have left home may prefer to live in a smaller house which a growing family would prefer to vacate. But the stamp duty could deter both of them from moving. Stamp duties may also encourage first home buyers to buy a larger house than they need at the time to avoid paying further duty should they require a larger home as their family grows.[12]

6.14 HomeStart Finance pointed to the difficulties stamp duty created for low to moderate income first home buyers. Stamp duty, it argued, is regressive in the sense that:

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7 Real Estate Institute of Australia, *Submission 88*, p. 14. Also see Mr Liam Foley, Policy Officer, Urban Development Institute of Australia, *Proof Committee Hansard*, 30 July 2014, p. 72.

8 Residential Development Council, Property Council of Australia, *Submission 212*, p. 13.

9 Honorary Associate Professor Judith Yates, University of Sydney, *Submission 53*, p. 6.

10 Australian Housing and Urban Research Institute, *Submission 93*, p. 7.

11 Urban Development Institute of Australia, *Submission 190*, p. 12.

12 Mr John Hawkins, *Submission 105*, p. 3.

> …the most vulnerable customers—low-moderate income first home buyers—are least able to afford it, or afford to save for it. The imposition of this tax at the time of purchase creates a significant disincentive both for first home buyers and overall property market transactions.[13]

6.15 The HIA drew the committee's attention to the fact that stamp duty is often applied multiple times along the process of a new home being brought to market: at the point of sale of land to developer, the sale of land from the developer to the builder, and the final sale of a house and land package to a purchaser. The HIA noted:

> This transaction and taxation process which can apply to the new home building sector is essentially treating new housing as 'trading stock' and is unique to this sector. In other industries, for example the used car industry, the 'commodity' is regarded as holding stock and does not attract stamp duty until the sale to the ultimate consumer. For the new home building sector, the taxes paid whilst approvals are being sought during the development phase can be significant and should be addressed by either a cut in rates or an exemption.[14]

State government land taxation

6.16 Witnesses also provided evidence suggesting that more broadly applied land taxes might help improve housing affordability, or at least provide a more efficient form of taxing housing than stamp duties.

6.17 In Australia, land value taxes are levied at the state and territory level. As the Henry Review explained, there are currently three taxes on land in Australia:

> The first is property conveyance duties (stamp duties) levied on the transfer of land and buildings. In 2007–08 they raised $14.4 billion for State governments. A significant proportion of this revenue is raised on the transfer of building values, rather than of land. The second is local government rates levied on land (and also on building values by some councils). They raised $10.2 billion in 2007–08. Finally, State government land tax (mostly levied on unimproved land values) raised around $4.3 billion in 2007–08.[15]

6.18 For the purposes of this chapter, 'land tax' is taken to refer to state government land tax, unless otherwise specified.

6.19 All jurisdictions except the Northern Territory levy land tax, and depending on the jurisdiction the calculation is based on either the 'unimproved' or 'site' value of the land. While the rate of land tax varies from state to state, it is generally only levied on commercial and investor-owned residential land. Owner-occupied land is exempt from land tax in all jurisdictions. As the Henry Review noted, the exemption of

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13 HomeStart Finance, *Submission 72*, p. 16.

14 Housing Industry Association, *Submission 178*, p. 7.

15 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), p. 251.

owner-occupied housing 'removes around 60 per cent of land by value from the tax base'. The Henry Review concluded that the exemption:

> …is likely to have particular influence on land for residential property. The exemption of owner-occupiers rules out around 75 per cent of residential land and, for the remainder, high thresholds in some States effectively exempt many small-scale investors. As land can shift in and out of the tax base depending on who owns it, it is unlikely that the tax will be fully reflected in lower land prices for residential property. The portion of tax that is not reflected in lower land prices is borne by investors through lower returns, or by their renters through higher rent. This means the tax, to some extent, has been passed forward to workers and the owners of capital. Further, it is likely that, in the long run, much of the burden of the tax is shifted to renters, as rents adjust to ensure that investors achieve an adequate return. This may be inequitable, as renters generally have low income and wealth.[16]

6.20 Other submitters, including the Tenants' Union of NSW, suggested that the exemption of owner-occupied housing from land tax encouraged overinvestment in owner-occupied housing.[17] Professor Frank Stilwell argued that a uniform land tax applied to the value of all land would help 'drive out the speculative element of the market', thereby bringing land price inflation under control:

> Indeed, if the government captured the economic surplus that is currently privately appropriated by landowners, it would only make sense for people to hold land for its use value—whether for housing, agricultural or other commercial purposes. There could then be no significant speculative gain, and land ownership would not be a vehicle for capital accumulation. Land price inflation would then be relatively stabilized.
>
> The current forms of land tax implemented by State governments do not achieve this outcome because the land tax rates are low and the exemptions are very extensive. A more comprehensive, nationwide land tax system would need to replace or supplement these State taxes.[18]

6.21 Mr Cameron Murray also argued in favour of land tax reform, suggesting:

> Increasing taxes on land in proportion to its value at its highest and best use provides enormous incentives to construct new housing even if it reduces rents and prices.[19]

6.22 For his part, Professor Dodson suggested that a more sophisticated land tax system would be able to capture the increase in land values, and redistribute it for 'infrastructure or affordable housing purposes'.[20]

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16 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), pp. 260–61.

17 Honorary Associate Professor Judith Yates, University of Sydney, *Submission 53*, p. 7; Tenants' Union of NSW, *Submission 120*, p. 13.

18 Professor Frank Stilwell, *Submission 25*, p. 4.

19 Mr Cameron Murray, *Submission 17*, pp. 6–7.

6.23 AHURI also noted that, in varying measures depending on the jurisdiction, land tax is only levied on the value of the land of investment properties above a certain threshold. For example, in Victoria land tax only applies on the excess value of $250,000 of rental properties held by an investor. This arrangement, it suggested:

> …is potentially responsible for the lack of large property investors in Australia. Residential property investment is characterised by a dominance of 'mum and dad' investors who mainly own one investment property (Berry 2000). In 2006–07, 1,542,712 individuals declared an interest in at least one rental property; 77 per cent had an interest in only one rental property and 91 per cent in one or two properties...[21]

Possible stamp duty and land tax reforms

6.24 The Henry Review recommended the removal of stamp duties and, in recognition of the revenue needs of the states:

> …a switch to more efficient taxes, such as those levied on broad consumption or land bases. Increasing land tax at the same time as reducing stamp duty has the additional benefit of some offsetting impacts on asset prices.[22]

6.25 The Henry Review further recommended that given the efficiency benefits of a broad land tax, 'it should be levied on as broad a base as possible.'[23]

6.26 Both the UDIA and the REIA recommended replacing stamp duty with 'more efficient' taxes, such as a broader GST.[24] While arguing in favour of abolishing stamp duty, the REIA took issue with the Henry Review's recommended replacement of stamp duty with a broad-based land tax:

> The Henry Review recommended that a land tax was an efficient means of replacing the revenue forgone from abolishing state stamp duties. In reality this is not the case. In practice it is likely that a significant proportion of the economic incidence of the tax is passed forward to consumers or backwards to investors adding distortions and reducing the efficiency of the tax and detracting from the claimed simplicity, equity and sustainability of the tax.[25]

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20 Professor Jago Dodson, Professor of Urban Policy, RMIT University, *Proof Committee Hansard*, 9 September 2014, p. 13.

21 Australian Housing and Urban Research Institute, *Submission 93*, p. 8.

22 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), p. 263.

23 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), p. 263.

24 Urban Development Institute of Australia, *Submission 190*, p. 5; Ms Amanda Lynch, Chief Executive Officer, Real Estate Institute of Australia, *Proof Committee Hansard*, 30 July 2014, p. 72.

25 Real Estate Institute of Australia, *Submission 88*, p. 14.

6.27 While acknowledging that stamp duty is a major source of revenue for state governments, the HIA maintained that it is nonetheless a 'highly inefficient tax'. It suggested the:

> …implementation of reforms which remove inefficient taxes that specifically affect housing, such as stamp duty on conveyancing, and replace the government revenue with more efficient taxes, improve housing affordability. Furthermore, such reforms are also likely to have broader economic benefits that deliver higher living standards to Australian households.
>
> A national tax reform agenda should develop a strategy and timeframe to replace stamp duty with more efficient taxes such as a broader based and/or higher rate of GST or a well-designed land tax. A Federally-led tax reform strategy is the only option for ensuring such change occurs.[26]

6.28 AHURI argued that replacing stamp duties with reformed land taxes would improve the efficiency of the housing market and housing affordability generally. Such reforms would:

> …speed up development in areas that are more expensive and reduce land values in the inner cities making purchases in these areas cheaper...[27]

6.29 Mr Eslake also called for a shift from stamp duties to broad-based land taxation, with a view to encouraging the more efficient use of land:

> That would include replacing stamp duty on land transfers (which are 'bad' taxes on many grounds, including that they discourage people from changing their dwellings as their needs change) with more broadly-based land taxes (ie, no exemptions for owner-occupiers, but with appropriate transitional provisions) and possibly higher rates for undeveloped vacant land in established urban areas.[28]

6.30 AHL Investments Pty Ltd ('Aussie') recommended a reduction in stamp duty over time, potentially shifting to a broad property tax to replace the revenue lost by state and territory governments. Aussie suggested, however, that this transition would:

> …need to be progressively implemented to minimise the impact on existing property owners. This would require special consideration to be given to houses of lower value and to those that have recently paid stamp duty under a different rate regime.[29]

6.31 Prosper Australia recommended abolishing stamp duties and implementing a broad-based land tax that should be levied at a federal level and then fully rebated to

26 Housing Industry Association, *Submission 178*, p. 7.

27 Australian Housing and Urban Research Institute, *Submission 93*, pp. 20–21.

28 Mr Saul Eslake, *Submission 2*, p. 15.

29 AHL Investment Pty Ltd (Aussie), *Submission 186*, p. 4.

the states.[30] Appearing before the committee, Prosper Australia was asked how a land tax would apply in situations where an income-poor person owned a family home on high-value land. The example of a pensioner sitting on $1 million block of land but not earning any income from it was put to Prosper Australia, and whether a land tax would price that pensioner out of her home. Mr David Collyer, Prosper Australia's Policy Director, replied:

> Not necessarily. We, collectively, could remove the burden from her either by deferring it or by increasing pensions if that proved to be an issue. You cannot do these things in isolation. The idea is not to impose a new tax on everybody and not change other taxes. The purpose of a land tax is to give you the opportunity to remove other taxes that we know are very bad for us. We are not trying to increase the government tax take; we are trying to rebalance or reposition taxation.[31]

The phasing out of stamp duty in the ACT

6.32 As noted by Mr Hawkins, while state and territory governments have generally not embraced stamp duty or land tax reform in response to the Henry Review, the ACT Government has moved to replace stamp duties over time with 'more efficient and fairer charges on land values'.[32] Following the Henry Review, the ACT Government in fact conducted its own taxation review, with the final report released in May 2012. Like the Henry Review, the ACT Taxation Review was highly critical of stamp duty:

> This tax is fundamentally unfair, in that it raises around a quarter of the total taxation revenue of the Territory from around 9 per cent of the people whose circumstances may impose the necessity to move to different accommodation. For this tax, around 38 cents of the economic value is lost for every dollar raised.[33]

6.33 The ACT Taxation Review recommended that stamp duty be abolished, with the revenue replaced by a broad-based land tax. The Review further recommended the application of a transition period of 10 to 20 years, 'to ameliorate the impact of the change on households'.[34] Subsequent to the Review, the ACT Government announced that it would abolish stamp duty over a 20 year period starting from mid-2012, with

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30 Mr David Collyer, Policy Director, Prosper Australia, *Proof Committee Hansard*, 9 September 2014, pp. 2–4.

31 Mr David Collyer, Policy Director, Prosper Australia, *Proof Committee Hansard*, 9 September 2014, p. 5.

32 Mr John Hawkins, *Submission 105*, p. 3.

33 ACT Government, *ACT Taxation Review* (May 2012), p. 3.

34 ACT Government, *ACT Taxation Review* (May 2012), pp. 7–8.

the revenue foregone to be replaced by an increased land tax (in the form of general rates, which the ACT Government, unlike other states and territories, levies itself).[35]

Committee view

6.34 The committee believes stamp duties are an inefficient, productivity-damaging form of taxation, which ultimately increase barriers to home ownership. As has been established across multiple inquiries and reviews, including the Henry Review, stamp duties discourage land from being allocated to its most efficient use, distort housing choices and undermine housing affordability. The committee also notes evidence that stamp duties reduce peoples' choice and flexibility in relation to their housing situation—including to downsize as circumstances change, move closer to work, and so on. This, in turn, damages labour mobility and hurts economic productivity more generally.

6.35 Currently, stamp duties constitute a significant source of revenue for the states and territories, and it would be unrealistic and even irresponsible to advocate their abolition without acknowledging that a replacement source of revenue would be required. The committee considers the Henry Review recommendations a good foundation for discussion on the need to move from stamp duties to broader, more efficient forms of taxation. As part of this discussion, the committee believes that states and territories should consider broadening the base of existing land taxation.

6.36 The committee further notes that such issues will likely be addressed in the forthcoming Tax White Paper. On the assumption that it is likely the White Paper will also underline the inefficiencies associated with stamp duties, the committee acknowledges that that the White Paper's authors may be better positioned to recommend reform directions. With this caveat in mind, the committee notes that it has heard no compelling arguments for maintaining stamp duties in their current form. On the basis of evidence received, the committee also believes that the phasing out of stamp duties should probably occur in tandem with land tax reforms so that the impact to state revenue is neutralised.

6.37 Beyond the political challenge of any transition from stamp duties to broad-based land taxation, the committee acknowledges that such changes would likely involve significant equity issues, not least for 'asset rich, income poor' households and retirees. This in itself is no reason to eschew reform in this area. The ACT Government's recent stamp duty reforms may provide a template—or at least a starting point—that other governments might consider in pursuing stamp duty reform. Moreover, while issues of equity are not insignificant, they are by no means insurmountable. Mechanisms for deferring land tax liabilities, or exemptions for owner-occupiers who would be unfairly affected by a broadening of the tax, are

35 John A. McLaren, 'The Australian Capital Territory has adopted measures to abolish stamp duty and impose a land tax on all real property: will this approach be adopted by other states in Australia?' *Journal of the Australasian Tax Teachers Association* 8, No. 1 (2013), pp. 101-116.

available to governments. Indeed, liquidity relief provisions that allow for the deferral of land value tax liabilities are already sometimes used in relation to local government rates.

6.38 Meaningful reform is difficult, but it is no less important for being so. The committee believes that if the will exists, it will be possible to phase out stamp duties in a way that is revenue neutral, equitable and has a positive impact on housing affordability.

6.39 While reform in this area is in the final analysis a matter for the states and territories, the committee believes the Commonwealth needs to engage with (and, as appropriate, provide leadership to) the states and territories in a coordinated reform process. This engagement would be based on a recognition that the implementation of such reforms should ideally take place as part of a broader process of taxation reform, possibly in response to the Tax White Paper.

Recommendation 5

6.40 The committee recommends that state and territory governments phase out conveyancing stamp duties, and that as per the recommendations of the Henry Review, this be achieved through a transition to more efficient taxes, potentially including land taxation levied on a broader base than is currently the case.

Infrastructure charges on new housing developments

6.41 For new housing developments, the costs of supplying infrastructure are substantial, and often add significantly to the price paid by the homebuyer. The question of who should bear these costs, and how and when, was raised by a number of witnesses. For many, current infrastructure charging regimes, as administered by state and local governments, appeared inequitable and inefficient.

6.42 Infrastructure charges, as defined in the final Housing Supply and Affordability Reform (HSAR) report produced by the intergovernmental HSAR Working Party, are:

> …fees levied on developers (or purchasers in some instances) by local government as well some state governments to fund basic (or nexus) infrastructure (such as local roads and water mains) necessary for land development. In some instances, infrastructure charges are also levied for major infrastructure (arterial roads and pumping stations) and social infrastructure (parks and libraries). Local councils are generally empowered through planning and development legislation to collect contributions from developers for infrastructure.
>
> There are two main types of infrastructure: 'social' and 'economic'. Economic infrastructure can be further categorised as 'basic' or 'major/trunk' infrastructure. Who pays for the infrastructure, and how, should be

> determined by the type of infrastructure and whether the costs can be accurately apportioned to those who benefit from the infrastructure.[36]

6.43 In its submission, AHURI explained how developers were required to cover infrastructure costs (directly or indirectly), and how in turn these costs added to the overall costs of new housing:

> Developers may be required to pay significant levies and contributions to councils either for basic infrastructure (such as roads, water, sewerage, gas and electricity connections), which may be constructed by the developer and handed over to the relevant authority, or for costs incurred by the local government in providing new infrastructure, or by requiring developers to contribute land for public open space or facilities.
>
> Developer infrastructure contributions represent the largest quantifiable planning related cost in Australia, exceeding $100 000 per lot in designated metropolitan growth areas of NSW and around $45 000 per lot in parts of Queensland (Gurran et al. 2009). These costs have increased markedly in a number of capital cities—in Sydney they have increased from around 3.5 per cent of the cost of a house price in the mid-1980s to 16.9 per cent in 2007 (Gurran et al. 2009).[37]

6.44 In their joint submission, Mr Borrowman, Associate Professor Frost and Dr Kazakevitch also pointed to research that quantified the costs associated with the shift towards user-paid infrastructure funding approaches in new housing developments. This research showed the cost burden was particularly pronounced in Sydney:

> Hsieh, Norman, and Orsmond (2012) estimate that in 2010 government charges (excluding GST) levied on developers amounted to around $60,000 per greenfield dwelling in Sydney, and between $20-30,000 per greenfield dwelling in other cities.[38]

6.45 The UDIA told the committee that the current means of funding infrastructure placed the cost burden on the new homebuyer up-front, when in fact that infrastructure had a long-lasting benefit to the community as a whole. The issue, it argued, was one of equity, balance and transparency.[39] Similarly, Aussie argued that under current infrastructure funding regimes, the initial purchasers were in effect required to fund

36 COAG Housing Supply and Affordability Reform Working Party, final report, *Housing Supply and Affordability Reform* (July 2012), p. 14.

37 Australian Housing and Urban Research Institute, *Submission 93*, p. 7.

38 Dr Gennadi Kazakevitch, Associate Professor Lionel Frost and Mr Luc Borrowman, *Submission 23*, p. 7.

39 Mr Liam Foley, Policy Officer, Urban Development Institute of Australia, *Proof Committee Hansard*, 30 July 2014, p. 67.

the benefits of future residents.[40] Dr Lawson and Professor Berry also expressed concern regarding:

> …the high development costs of new housing on a constrained urban fringe, where revenue strapped local governments lack the capacity to develop infrastructure in advance. Upfront development fees directly impact 'first generation' purchasers, rather than being shared across a wider spatial area and longer time frame.[41]

6.46 In its submission, the HIA provided a detailed argument against existing arrangements for funding social and community infrastructure through what it regarded as a 'complex array of levies charged throughout the residential development process'. In doing so, the HIA drew a distinction between 'development-specific infrastructure items' within the boundaries of a development, such as local roads, drainage, sewerage, power supplies and so on—which it agreed should be provided by the developer as part of the cost of development—and community and regional infrastructure which is 'ancillary to the direct provision of housing for a larger population and provides a benefit to the broader community'. This latter category, the HIA argued, should not be funded by developer contributions:

> The excessive costs levied from the developer are passed on to new homebuyers who in effect partially or wholly fund infrastructure items from which the whole community derives benefit. The cost of community infrastructure should be met by general revenue rather than an inequitable tax levied on new homebuyers.
>
> Removal of the excessive infrastructure charges incurred during the production of new homes will lower the final purchase price to consumers, thereby improving the relative cost differential between new and established housing and increasing demand for new homes. The additional supply of housing would assist to restore the housing supply imbalance.[42]

6.47 The UDIA argued that developer contributions should be 'charged proportionately to the benefit received by the beneficiary of the infrastructure, and should be transparent in their calculation and application'. It suggested that currently this was often not the case, with excessive infrastructure charges undermining housing affordability:

> Developer contributions are frequently opaque and unjustified in their application, and there may be no clear connection between the cost of the infrastructure provided and the contribution, to the extent that the contribution may be well in excess of the cost of the infrastructure it is supposed to pay for. Additionally in many cases developer contributions are used to pay for infrastructure that benefits the wider community (for

40 AHL Investments Pty Ltd, *Submission 186*, p. 4.

41 Dr Julie Lawson and Professor Mike Berry, Centre for Urban Research, RMIT University, *Submission 24*, p. 7.

42 Housing Industry Association, *Submission 178*, pp. 7–8.

> example trunk roads and utilities infrastructure upgrades). In this case, developers and ultimately new home buyers are being forced to subsidise the rest of the community.[43]

6.48 The UDIA argued that a further problem with current approaches to infrastructure funding was that sometimes there was an incentive for local governments to:

> …set unnecessarily high engineering and construction standards in order to minimise their ongoing maintenance and replacement costs. Where these reduced costs aren't reflected in lower council rates, new home buyers effectively end up paying for their infrastructure twice, once through a higher up front house price, and again through recurring rates.[44]

6.49 According to Mr Eslake, state and local governments' policies for charging for the provision of suburban infrastructure were a key reason for the failure of the housing stock to keep pace with population growth in recent years. These policies, Mr Eslake suggested, 'have made it increasingly difficult for the private sector to supply new housing, especially at the more affordable end of the spectrum'. In particular, onerous requirements on developers for the provision of infrastructure and services in new housing estates, and the shift from a debt-financed to up-front model of funding this infrastructure, had priced home buyers out of developments that would otherwise be affordable:

> While this is consistent with a 'user pays' philosophy, and appeases the growing voter aversion to public debt, it has meant (especially in New South Wales, where developer charges have risen to much higher levels than in other States) that developers find it increasingly difficult to produce house-and-land packages at prices which are affordable for first-time buyers and still make a profit, so they have reacted by building a smaller number of more expensive houses targeted at the trade-up market.[45]

6.50 JELD-WEN argued that the high fees and charges on new land purchases, many of which had been imposed in the years since 2000, had:

> …distorted home buyer preferences away from job-generating new housing to established housing. In the mid-1990s, more than a quarter of owner-occupiers opted for a new dwelling; by the late 2000s, the share of purchases for new housing had almost halved.[46]

Proposals for new approaches to infrastructure funding

6.51 Professor Beer explained that in New South Wales, Victoria and Queensland the homebuyer will pay substantial amounts toward off-site infrastructure, an

43 Urban Development Institute of Australia, *Submission 190*, pp. 12–13.

44 Urban Development Institute of Australia, *Submission 190*, p. 13.

45 Mr Saul Eslake, *Submission 2*, pp. 5–6.

46 JELD-WEN Australia, *Submission 54*, p. 7.

approach which on the one hand adds to housing costs, but on the other ensures the adequate provision of infrastructure. In South Australia, however, the opposite situation prevailed, where in many cases no adequate infrastructure was provided. Professor Beer suggested new thinking was required as to how 'we can finance infrastructure over the life of the property rather than putting all the costs either on the general taxpayer or on the first home buyer'.[47] Professor Beer suggested, for example, that local councils should be able to raise bonds to fund infrastructure:

> They can raise a bond—which obviously they get at a very low rate relative to some forms of commercial credit—which they can pay off over time. So, there is intergenerational equity, because it is not the first generation of home purchasers who have to pay that enormous cost; it is actually spread over the 20, 30, 40 or 50 years of the life of that infrastructure. It is equitable spatially, because those who are living at the fringe and choosing to move into that housing and are getting the benefit of that new housing pay for it. It can also be equitable for those living in the city areas, because they are not paying for it and also, if they are going through a process of urban regeneration, they can actually create their own bond and pay for the redevelopment of their urban infrastructure in ways that may be needed by using a similar sort of device. And it is not one generation that pays for it, because they are not the only generation to benefit.[48]

6.52 Similarly, Mr Michael Basso argued that the shift toward developers paying for infrastructure in new estates, rather than local councils, had:

> …a significant impact on the price of land, which has flowed through to the cost of existing properties, pushing prices up across the board. Developers obviously build these infrastructure costs into their prices meaning buyers need to pay significantly more upfront, money that will generally be borrowed and cost them significantly more in interest over time. Given the flow-on effect into existing house prices, every property buyer is essentially paying this extra amount in perpetuity and this is ultimately ending up in the banks' coffers through interest charged on the loans. It would make a lot more sense for councils to absorb this cost through some form of development bond and have residents repay the cost through council rates.[49]

6.53 While much of the evidence received was focused on the costs imposed on developers by current infrastructure charging arrangements—and in turn the impact this had on housing prices—the Brisbane City Council argued that it was required to bear much of this cost itself. Specifically, the Council told the committee that the imposition of state-wide regulated maximum infrastructure charges in Queensland

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47 Professor Andrew Beer, Director, Centre for Housing, Urban and Regional Planning, University of Adelaide, *Proof Committee Hansard*, 28 July 2014, p. 16.

48 Professor Andrew Beer, Director, Centre for Housing, Urban and Regional Planning, University of Adelaide, *Proof Committee Hansard*, 28 July 2014, pp. 20–21.

49 Mr Michael Basso, *Submission 209*, p. 5.

placed the Council under considerable fiscal pressure.[50] It suggested that under the prevailing arrangements in Queensland, the Council was effectively subsidising infrastructure costs:

> At the present time, council subsidises new house lots by an average of some $10,000 to $15,000. The standard charge has been set across the state at $28,000 by the state government. We are currently charging $27,000 per allotment. As I said, we believe the user pays charge would be in the order of about $35,000 for a lot of housing but in some parts of Brisbane the user pays charge is in the order of $55,000 to $65,000. So in that regard we are subsidising development using general rates revenue. While it does add to the cost of housing, without the supply of essential infrastructure such as water, sewerage and access to transport, there is no product that can be sold so it is something that really adds value. If it is not there, the development has no value whatsoever.[51]

6.54 The HIA suggested that alternative infrastructure funding mechanisms could provide better affordability outcomes for new home buyers. Mechanisms suggested by the HIA included government infrastructure bonds and the Tax Increment Financing model, wherein government is able to draw tax revenues from increases in value within prescribed Tax Increment Financing areas to cover the up-front costs of infrastructure.[52] Mr Eslake also suggested that an alternative approach to infrastructure funding might to use 'levies on the increments to the value of the land which result from such investments'.[53]

6.55 Youth Action NSW referred to the McKell Institute 2012 report, *Homes for All*, which argued that the levies and charges charged to developers by local governments were, in Youth Action NSW's words, 'dramatically impacting on the housing supply in New South Wales'.[54] Drawing on the McKell Institute's report, Youth Action NSW argued:

> Tax Increment Finance (TIF) schemes should be implemented in order to redistribute infrastructure costs. A TIF scheme allows local authorities to borrow money in order to advance infrastructure growth. The money can be

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50 These limits are set out in Department of State Development, Infrastructure and Planning, *State Planning Regulatory Provision (adopted charges)* (July 2012), http://www.dsdip.qld.gov.au/resources/laws/state-planning-regulatory-provision/sprp-ict.pdf.

51 Mr Kerry Doss, Manager, City Planning and Economic Development, City Planning and Sustainability Division, Brisbane City Council, *Proof Committee Hansard*, 10 September 2014, p. 2.

52 Housing Industry Association, *Submission 178*, pp. 9–10. On TIF, see PriceWaterhouseCoopers, draft report for the Property Council of Australia, 'Tax Increment Financing to fund infrastructure in Australia' (April 2008), http://www.infrastructureaustralia.gov.au/public_submissions/published/files/486_propertycouncilofaustralia_sub2.pdf.

53 Mr Saul Eslake, *Submission 2*, p. 15.

54 Youth Action NSW, *Submission 51*, pp. 81–82.

> sourced from the public or private sector. The construction of infrastructure will increase site values and local tax revenues, along with providing incentives for local communities to support growth.[55]

6.56 In order to improve equity and affordability outcomes, the UDIA recommended that governments:

> …favour funding and financing approaches that spread the cost of infrastructure out over extended time frames, rather than impose it up front, such as through developer contributions.[56]

6.57 Similarly, BIS Shrapnel argued that the cost of infrastructure associated with new development is often borne by developers and thus new residents, despite the benefit being enjoyed by the broader community. It argued:

> A shift in focus could result in a more equitable sharing of infrastructure costs across all who benefit from them. There exists a role for government to play in funding and providing the necessary infrastructure here and the right balance must be struck between developers and government as to who foots the bill. This would help reduce developer contribution costs and thus help limit the ultimate cost of new housing development.[57]

Previous reviews of infrastructure charges

6.58 It should be noted at this point that the issues raised in this inquiry regarding infrastructure charges have been covered extensively in previous review processes, including the HSAR final report and the Henry Review.

6.59 The Henry Review addressed infrastructure charges in some detail. It found that infrastructure charges 'can be an effective way of encouraging the efficient provision of infrastructure where it is of greatest value and of improving housing supply'. However, it also found that poorly administered infrastructure charges—particularly charges that are complex, non-transparent or excessive—'can discourage investment in housing, which can lower the overall supply of housing and raise its price'. The Henry Review recommended that COAG review infrastructure charges to ensure they were transparent and 'appropriately price infrastructure provided in housing developments'.[58]

6.60 The issue of infrastructure charges was subsequently reviewed by COAG's HSAR Working Party. In 2012, COAG agreed to the recommendation made in the HSAR final report that infrastructure charges should be consistent with four principles agreed by the HSAR Working Party, covering efficiency, transparency and accountability, predictability, and equity (as outlined below). COAG also agreed to

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55 Youth Action NSW, *Submission 51*, p. 84.

56 Urban Development Institute of Australia, *Submission 190*, p. 5.

57 BIS Shrapnel, *Submission 16*, p. 3.

58 Treasury, *Australia's Future Tax System Review final report* (Canberra 2010), pp. 423–29.

note the best practice guidelines for applying the infrastructure charging principles, as developed by the HSAR Working Party.[59]

6.61 The HSAR report suggested that infrastructure charges should only be used when infrastructure serviced a particular development, or when the infrastructure serviced a number of developments but it was nonetheless possible to apportion costs based on the demand each development placed on the infrastructure. It suggested that infrastructure should be funded through general revenue in the instance it serviced a number of developments, and it would be 'extremely difficult or not possible to accurately apportion the costs because the benefits of the infrastructure are widely distributed'. It also suggested that such charges should not be levied in cases where direct user charges could be applied.

6.62 The final report recommended that to the extent infrastructure charges were used, they should at least be:

- *efficient*—charges should be for infrastructure required for the proposed development or for servicing a major development;
- *transparent and accountable*—charging regimes should be supported by publicly available information on the infrastructure subject to charges, the methodology used to determine charges and the expenditure of funds;
- *predictable*—charges should be in line with published methodologies and charging schedules (with clarity around the circumstances in which charges can be modified after agreement); and
- *equitable*—where the benefits of infrastructure provision are shared between developers (land owners), the infrastructure charges levied on the developer should be no higher than the proportional demand that their development will place on that infrastructure.[60]

Committee view

6.63 The committee notes that many of the issues raised and recommendations made by witnesses in this inquiry regarding infrastructure charges have been canvassed in previous inquiry reports, including the Henry Review and the HSAR final report that COAG agreed to in 2012. The committee also recognises that the question of how infrastructure is funded raises complex equity issues. Expressed in the most basic terms, these issues come down to who should pay for new infrastructure and when they should pay it: should new home buyers bear the cost,

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59 COAG Housing Supply and Affordability Reform Working Party, Final Report, *Housing Supply and Affordability Reform* (July 2012), pp. 14–15. The best practice guidelines are included in the final report at Appendix B. COAG agreed the report recommendations out-of-session in July 2012. https://www.coag.gov.au/node/451.

60 COAG Housing Supply and Affordability Reform Working Party, Final Report, *Housing Supply and Affordability Reform* (July 2012), p. 15.

either up-front or over time? Or should the broader community bear the cost, particularly when it is established that the benefits from that infrastructure are shared by the wider community?

6.64 There are no simple answers to these questions. However, the committee does note that the final HSAR report recommended that COAG agree to the HSAR Working Party's four principles for infrastructure charges—efficiency, transparency and accountability, predictability, and equity—and that COAG note the associated best practice guidelines produced by the Working Party. In light of COAG agreeing to this recommendation, the committee believes it would be beneficial for state and territory governments to report through COAG (and preferably through the recommended ministerial council for housing and homelessness) on what changes, if any, they have since made to ensure infrastructure charges are consistent with these four principles. This would help ensure that progress is being made in this area, and encourage transparency, information sharing and the take-up of best practice approaches to infrastructure charges.

6.65 Several submitters raised the possibility of using Tax Increment Financing or bonds to fund infrastructure in new housing developments. The committee believes that, if nothing else, alternative approaches to infrastructure funding may merit further consideration by state and local governments.

Recommendation 6

6.66 The committee recommends that all states and territories report to the Council of Australian Governments (COAG), preferably through a new ministerial council on housing and homelessness (see recommendation 2), on what policy changes, if any, have been made to ensure infrastructure charges are consistent with the four principles agreed through COAG in July 2012.

Recommendation 7

6.67 The committee recommends that state and local governments investigate the possibility of using Tax Increment Financing and other innovative finance mechanisms to fund infrastructure for new housing developments.