HOUSING INDUSTRY ASSOCIATION

Submission to
Icon Water

Water and Sewerage Capital Contributions Charge

17 March 2017

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contents

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ABOUT THE HOUSING INDUSTRY ASSOCIATION

The Housing Industry Association (HIA) is Australia's only national industry association representing the interests of the residential building industry, including new home builders, renovators, trade contractors, land developers, related building professionals, and suppliers and manufacturers of building products.

As the voice of the industry, HIA represents over 30,000 member businesses throughout Australia, with over 1,200 members in the ACT and Southern NSW. The residential building industry includes land development, detached home construction, home renovations, low/medium-density housing, high-rise apartment buildings and building product manufacturing.

HIA members comprise a diversity of residential builders, including large volume builders, small to medium builders and renovators, residential developers, trade contractors, major building product manufacturers and suppliers and consultants to the industry. HIA members construct over 85 per cent of the nation's new housing stock.

HIA exists to service the businesses it represents, lobby for the best possible business environment for the building industry and to encourage a responsible and quality driven, affordable residential building development industry. HIA's mission is to:

> *"promote policies and provide services which enhance our members' business practices, products and profitability, consistent with the highest standards of professional and commercial conduct."*

The residential building industry is one of Australia's most dynamic, innovative and efficient service industries and is a key driver of the Australian economy. The residential building industry has a wide reach into manufacturing, supply, and retail sectors.

The aggregate residential industry contribution to the Australian economy is over $150 billion per annum, with over one million employees in building and construction, tens of thousands of small businesses, and over 200,000 sub-contractors reliant on the industry for their livelihood.

HIA develops and advocates policy on behalf of members to further advance new home building and renovating, enabling members to provide affordable and appropriate housing to the growing Australian population. New policy is generated through a grassroots process that starts with local and regional member committees before progressing to the Association's National Policy Congress by which time it has passed through almost 1,000 sets of hands.

Policy development is supported by an ongoing process of collecting and analysing data, forecasting, and providing industry data and insights for members, the general public and on a contract basis.

The Association operates offices in 23 centres around the nation providing a wide range of advocacy and business support, including services and products to members, technical and compliance advice, training services, contracts and stationary, industry awards for excellence, and member only discounts on goods and services.

1. INTRODUCTION

This submission has been prepared by the Housing Industry Association (HIA) in response to the proposal by Icon Water to introduce new water and sewerage capital contributions charges across several parts of the ACT to fund the augmentation of aged and inadequate infrastructure to meet future urban growth.

The housing industry does not accept that the proposal to levy new home buyers is a legitimate means of funding network augmentation, which will deliver a broader economic and social benefit to the entire community. Governments (and publicly owned monopoly utilities) have a responsibility to implement infrastructure programs to sustainably support the anticipated population growth in a manner that ensures the investment, and the costs for such investment, is shared equitably across the whole community.

Up-front charges applied to development to fund community infrastructure significantly affect housing affordability. Such charges on development are the least efficient way to recover infrastructure costs and they are an inequitable means of funding long-lived community assets.

Development specific infrastructure which sits within the boundaries of a development, and provides essential access and service provision without which the development could not proceed, are rightly provided and paid for by the developer (and subsequently the new home owner) as part of the cost of development. However, broader community infrastructure that benefits the entire orderly functioning of the community and which provides a service for both existing and new residents, should not be funded solely by new home buyers.

Over recent decades there has been a shift by some state and territory governments, and public utilities towards funding public infrastructure through development levies. This approach has been in lieu of the traditional and more equitable reliance upon the whole of the community to support the ongoing delivery and maintenance of infrastructure and when required, the amplification of that infrastructure. Instead, this approach imposes significant cost on the minority of the community at any point in time, being new home purchasers.

Effectively, financing of public services is being transferred to the private purse. The unintended result of this approach also being to artificially increase house prices generating additional wealth for existing homeowners, at the expense of new home buyers.

The augmentation of the water and sewerage network that Icon Water has identified it needs to undertake over the next 20 years should now be factored in to the pricing policy for all water users. It is implausible for Icon Water to argue that the government's urban renewal and infill agenda has not been able to be planned for in a more measured and equitable manner than to simply apply an upfront levy to the smallest group within the community at any point in time, being new home buyers.

2. THE CASE FOR A NEW LEVY

2.1 PREVIOUS APPLICATION OF CHARGES

It is argued that this new charge is designed to replace an existing 'unfair' charging regime which means that developers will pay no charge if existing water and sewerage capacity exists in the local infrastructure, or alternatively, requires that the developer pays the full cost of a network-wide upgrade if insufficient infrastructure capacity exists. However, according to media reports,[1] the historical application of charges for augmentation of the water and sewerage network by Icon Water has not been an impost on industry around which the case is being built for a new levy.

The report refers to the Land Development Agency (LDA) and the National Capital Authority (NCA) both paying the charge – for the projects at the former Downer School and Constitution Avenue respectively – however, cannot cite instances where private developers have paid the charge.

It is acknowledged that Icon Water have attempted to answer this criticism through citing 'commercial-in-confidence' reasons for not referring to any private developers, and the extent that they may have paid the charge. On paper, this approach to charging for augmentation does appear to be inequitable. Nonetheless, in the absence of evidence to the contrary, it would appear that this new charge is, overall, an attempt to shift the cost burden for shared public assets onto the new home buyer.

Utility providers have a responsibility, and should have the ability, to accurately estimate the future population and the likely infrastructure network capacity required over a fixed period of time. Based on this information, those same providers should have the ability to apply the most equitable and transparent funding arrangement. To not do so would see these public agencies failing in a fundamental way to meet the public good they are intended to deliver. Whilst there may be an argument that the current model of financing future augmentation is not appropriate, the model that has been put forward is equally inappropriate.

2.2 SCOPE OF WORK

Despite requests from the building and development industry, directly, and through open consultation sessions, insufficient substantiating evidence has been provided to allow the public to fully assess the proposal. The information provided to date outlines areas to be affected and sets out an overall amount of funding required to support augmentation in those areas.

However there has been no detail provided during the consultation on the actual facilities, infrastructure upgrades or services that are included within the final amounts disclosed. The scope of augmentation work that will be funded by these levies is therefore unclear.

While developers, and therefore new home buyers, are being asked to fund these upgrades to community assets, there is scant information being provided as to what these charges relate to. Without providing an understanding to the industry of what specific assists these charges relate to, or a proposed sequencing plan for infrastructure upgrades is, it is unrealistic to expect support from the residential building industry. It is presumed this information must exist and has underpinned the calculations undertaken by Icon Water.

This information must be disclosed to facilitate further consultation on the levy.

[1] *Charges Still to Kick In*, The Canberra Times, 21 February 2017

3. HOUSING AFFORDABILITY

3.1 TAXATION ON HOUSING

In 2011 HIA commissioned an independent report[2] into taxation on new housing from the Centre for International Economics (CIE). Information on all the taxes that contribute to the final price of a new home were collated, with figures then verified with many residential building businesses.

When all taxes are included (direct and indirect), the taxation on a new house and land package in Sydney is an estimated 44% of the purchase price, for Melbourne the figure is 38% and for Brisbane the figure is 36%. The level of taxation of apartments was found to be comparable by CIE, being Sydney 35%, Melbourne 33% and Brisbane 34%. These figures have since been replicated in a further study conducted by CIE, which focused on smaller capital cities and regional centres.

The burden of tax falling on the housing sector is considerably higher than the average for all other sectors. New housing is inequitably taxed, accounting for around 1.2% of value added in the national economy while contributing 2.8% of government taxation revenues. The average tax burden on the new housing sector is estimated at 31% of the value of output compared with an economy-wide average of 24.4%. This percentage for new housing makes it the second most heavily taxed large industrial sector in the Australian economy.

Consequently, the taxation system influences the stock of dwellings available for occupation and the extent to which new housing is added to the stock. Appropriate policy settings will be crucial to ensuring that the ACT's housing meets the current and future needs of the population.

Several the taxes imposed on the housing sector, and on new housing are inefficient. The *Australia's Future Tax System* report[3], commonly referred to as the 'Henry Tax Review' found that among the vast array of taxes paid by the housing sector, about half of them were highly inefficient. The Henry Tax Review highlighted inefficient and excessive costs within infrastructure charges, such as is being considered by Icon Water.

3.2 HOUSING AFFORDABILITY IN THE ACT

After NSW and Victoria, the ACT is Australia's third most challenging jurisdiction in terms of housing affordability.[4] During the December 2016 quarter, affordability in the ACT deteriorated by 10.6% and was 8.3% less favourable than a year earlier.

Post the Global Financial Crisis (GFC), housing affordability in the ACT reached its most favourable position during the June 2015 quarter. Since then, the HIA Housing Affordability Index has declined from 88.4 to 76.6, equivalent to a deterioration of 13.3%. The change in affordability in the ACT over the past year is largely the result of significant growth in dwelling prices.

During the December 2016 quarter, the median dwelling price was $595,000, an increase of 13.2% on the same period a year earlier when the median price was $525,500.

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[2] *Taxation of the Housing Sector*, Centre for International Economics, September 2011

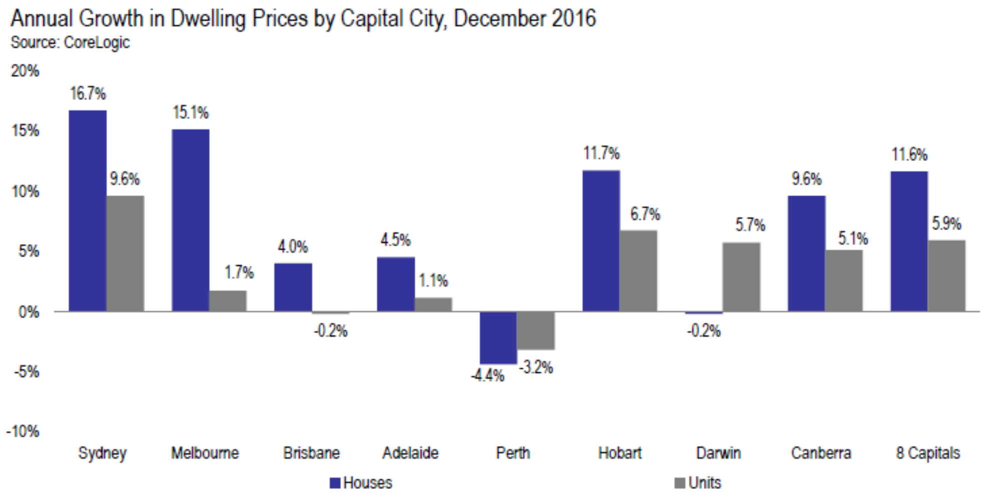
[3] *Australia's Future Tax System*, Henry, 2010

[4] *Housing Affordability Report*, Housing Industry Association, December 2016.

The relatively restricted financial state of the federal government and the prevalence of low inflation generally have constrained earnings growth in the ACT. Average earnings are estimated to have risen by 1.1% over the year to the December 2016 quarter.

Affordability conditions will continue to deteriorate if dwelling price growth continues to outpace earnings.

As can be seen in the following table, the annual growth in dwelling prices in the ACT over the past 12 months has been quite robust. If the inflationary impact of the proposed Icon Water charge was applied to the average rate of price growth in Canberra units, a $353,000 (pre-charge) unit in Woden would experience price growth of 7.06%, putting it only behind Sydney in terms of dwelling price growth for apartments.



3.3 IMPACT ON NEW HOME BUYERS

HIA is concerned that at a time when the ACT Government is acknowledging the challenges faced with respect to housing affordability in the Territory, and is pursuing policies to address this problem, that a charge which will be passed directly on to the community is being contemplated in lieu of a holistic approach to the funding of long lived infrastructure that supports the whole ACT community.

In the case of a two-bedroom unit, the Icon Water charge will be as follows across the four nominated precincts: Woden ($6,300); North Canberra ($3780); Fyshwick ($3,150); and, Belconnen ($2,940).

The example of a two-bedroom unit is being used as it is a common dwelling being constructed in Canberra, along with being a reasonable proxy for first home buyers, who make up a significant portion of the Canberra unit market.

The following table demonstrates the impact of the Icon Water charge on both repayments and purchase price.

Example: 2-bedroom unit in Woden

	Original loan	ICON Charge Woden	add GST	New loan
Loan size [5]	$353,000	$6,300	$6,930	$359,930
Loan term (years)	30			30
Interest rate	6.50%			6.50%
Monthly repayment	$2,231.20			$2,275.00
Increase in repayments				$43.80
Total over 30 years				**$15,768.83**

As the charge is levied prior to the settlement of a new dwelling contract, it will attract the Goods and Services Tax (GST), effectively creating a 'tax on a tax'. It is also worth noting Stamp Duty will be levied on the total contract price, however, given the concessional arrangements currently available in the ACT including to first home-buyers, it is not being included in the model. It would nonetheless apply to purchases by all other buyers, and in this example, a right-sizer couple would be faced with the additional tax on tax for the stamp duty component.

It is also worth noting that inflationary development levies such as the proposed Icon water levy, where passed onto home buyers will also have implications for the Loan to Value Ratio (LVR), and therefore the level of Lenders Mortgage Insurance (LMI) potentially charged to borrowers.

When the impact of the GST is included, the proposed Icon Water levy on its own negates the ACT First Home Owners Grant, which was reduced to $7,000 on 1 January 2017. This effectively represents a transfer of wealth via the grant from first home buyers to Icon Water, or the broader community if it is assumed that these public assets should be funded by the beneficiaries and not new home owners.

Using this same example, an alternative way of looking at the charge is that over the life of a loan, the home buyer must make almost $16,000 in additional mortgage repayments, based on a 30-year loan at an indicative long term interest rate. This is driven by an increase of forty-three dollars per month in payments.

3.4 DISPARITY WITH EXISTING HOMES

The proposal to levy this charge on new properties alone, further increases the disparity between new and existing properties. At present, new homes attract the GST, while existing properties do not. This adds to the cost of a new home versus existing properties, providing a competitive advantage to the latter. The construction of new homes provides employment within the community and generates activity in a number of other sectors such as professional services and retail.

Applying the Icon Water levy further discourages the construction of new dwellings to the benefit of existing property. This has the potential to have a negative impact on the ACT economy with respect to construction

[5] *Australian Property Investor Magazine*, median unit price Phillip ACT, January 2017

activity, at the same time as seeing less new dwellings constructed which will limit the base across which utilities such as Icon Water can amortise such costs.

Although Icon Water have stated that it will fund 50% of the cost of this infrastructure upgrade, via existing property water rates, it was noted in the consultation process that this contribution will be funded primarily through the additional rates in new developments. It is understood that the calculation does not include existing property water rates for homes built prior to the charge being introduced. This means that new home buyers in affected developments will fund up to 100% of the cost of network upgrades that are proposed, whilst all existing home owners will benefit from the augmentation works proposed.

4. IMPLICATIONS FOR GOVERNMENT

4.1 INCONSISTENCY WITH GOVERNMENT STRATEGIC PLANNING

The Icon Water charge runs counter to several well-entrenched ACT Government policies, with respect to urban renewal and infill development. ACT Government strategic planning documents state that for future development *"infill sites for increased density will have been identified for new housing. Increased density will help support more efficient public transport and vibrant neighbourhood centres."* [6]

The government's commitment with respect to light rail from both Gungahlin and Woden to the city and associated development along these corridors, and the recent release of the updated Belconnen town centre masterplan in September 2016 reflect this strategy. The Icon Water charge is in direct conflict with this strategy, introducing a significant disincentive to redevelopment in these areas. Icon Water itself points to this new charge as being a consequence of the government's aim to increase density, so it would create a perverse outcome if a charge levied to reflect government policy, in fact caused it to fail.

The ACT Planning system should create an environment where the private sector can innovate and deliver a range of housing types and styles to the community, within the boundaries set by the government and community's overall vision for the city. This charge contributes positively to neither. Setting significant and inconsistent price imposts on development will invariably drive development to occur where projects are feasible, rather than where is preferred.

Industry accepts that costs associated with the direct delivery of infrastructure to any redevelopment site will rightly be a development cost. However industry does not accept that developments should generically fund the greater augmentation of Canberra's existing water and sewerage system, which will continue to deliver services to all existing and future residents. While the government may favour 'infill' as a strategic aim, rather than having a preference for development in one centre over another, there is of course another option which is that projects simply do not proceed due excessive charges.

4.2 REDUCING GOVERNMENT REVENUE

When considering the proposed new water and sewerage charge, the impact on the value of land for development needs to be considered. As outlined in this submission, in an environment where demand for new housing outstrips supply, this charge will be passed on new home owners.

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[6] *ACT Planning Strategy: Planning for a sustainable city*, 2012.

However, should this market soften it would be likely that this charge would put downward pressure on the prices received for land, for example by the new *City Renewal Authority* along the Northbourne Avenue Corridor. The latest HIA housing forecast for the ACT[7] highlights a rebalancing between detached housing and multi-unit dwellings following a sustained period of construction of the latter.

Commencements for detached home building are expected to rise from 1,022 in 2015/16 to 1,848 in 2019/20, while multi-units are forecast to fall from a peak of 4,076 in 2015/16 to 2,488 in 2019/20, after bottoming out at 2,243 in 2017/18. Therefore, there is an existing downside risk to government revenue from land sales due to the current market environment already forecast within the current market. Any additional imposts on future development will only add further to this risk further.

5. CONCLUSION

HIA rejects the proposition that a levy on new home buyers to fund network wide capital upgrades is efficient, equitable or in the interests of the ACT community.

The charge being proposed is to augment existing community infrastructure, which by Icon Water's own description are 'shared assets' that service the wider population well beyond the proposed development.

As beneficiaries of the provision of new infrastructure the whole community should share the cost of that benefit. As the owner of an income producing asset that will have a life of many decades beyond the projected levy collection period, Icon Water should be considering funding mechanisms such as borrowings to be supported by water and sewerage rates or water pricing as the primary means of addressing this problem.

There has been some discussion around a reduced charge which covers a broader area, and applied to all new developments within the ACT. During the consultation process, Icon Water has estimated that this charge would equate to around $1,400 per EP when applied to all developments. HIA equally rejects this proposal.

For the reasons stated in this paper, such a charge is still inefficient and inequitable, and although this proposal addresses the distortionary impact of applying the charge at different rates across precincts, it is nonetheless a new tax on housing and job creation in the ACT.

Icon Water informed industry during the public consultation that the required upgrades to the network could be achieved with an increase of around 5% in existing water rates to all properties, existing and future. This minor impost on the entire community reflects a more equitable and economically efficient means of funding the upgrades of shared public assets.

The alternative being proposed is a levy on new home owners that could add up to $7,500 to the price of a townhouse, and require additional mortgage payments of over $15,000 for the life of a loan on a two-bedroom unit, which should be rejected.

[7] *ACT Outlook, Summer Edition*, HIA, March 2017.