

Submission on draft report

To:

The New Zealand Productivity Commission

Regarding:

Housing Affordability Inquiry - Draft Report: December 2011

Submitter:



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Submission

1. The opportunity to make this submission on the Housing Affordability Inquiry Draft Report (**the report**) is appreciated.
2. Civic Futures Ltd provides public sector agencies with advice and analysis on a range of regulatory matters connected with property development, growth modelling and funding and asset management. We have also worked on projects related to affordable housing. This submission is made by Greg Marr, Principal, on behalf of Civic Futures Ltd.
3. We would be happy to provide additional comment to the Productivity Commission (**the Commission**) on the matters covered in this submission.

1 Summary of submission

4. This submission:
 - Provides some preliminary comments related to the report as a whole and by way of context for the submission
 - Raises some concerns over the suggestion of introducing “merit based appeals” for development contributions (as a form of infrastructure charges)

- Provides comments the proposed to update the best-practice guidelines (and generally supports that approach; though notes including that in legislation might be premature)
- Provides further comments on a small number of specific parts of the report

2 Preliminary comments

5. The focus on housing affordability is important. Housing impacts on many parts of society, as set out by the Commission. This submission concentrates on development contributions and infrastructure funding issues.
6. The Commission, through the concerns that it raises about development contributions, portrays these as in need of amendment. While the Commission's views and analysis is more balanced than that prepared by others, they do continue a view that development contributions are being widely used in an improper way. As a preliminary point, we think it is important to note that there is limited evidence for that.
7. In contrast, we suggest that the available evidence points to development contributions being used, in the vast majority of situations, in a reasonable, lawful and considered way. In particular we note:
 - There have been a small number of court cases (3); two of these were concerned with fairly narrow interpretation issues of a couple of clauses in the Local Government Act 2002 (**the LGA**)¹. These cases have been accepted by all of the stakeholders and have not had to be re-litigated.
 - Many councils have put in place very significant efforts to enable their stakeholders, including the development community, to understand the policy, to understand the charges that result and to have policy input at an early stage (in addition to the formal statutory processes).
 - Councils have also undertaken several studies to understand the impact of contributions on their community (both existing and future communities), and have altered their policy direction where necessary.
 - Many councils across New Zealand (using different approaches and with different situations) have arrived at a "per-dwelling" contributions charge in the range \$20,000 to \$30,000; these charges cannot be considered unreasonable in the context of typical house prices.
 - The report indicates that contributions made up 4.5% of council's total revenue (p112); this must be seen as reasonable in the context of growth typically in the range 1% - 1.5% pa for many councils.
 - Many councils also have mechanisms in place to recognise and handle truly different (non-standard) developments.
8. Based on the above, we suggest that the development contributions system might need minor amendments at best, and is fundamentally working well for the majority of communities.

Development contributions do however involve some complexity, and a connection

¹ Specifically, *Domain Nominee Limited v Auckland City Council* (CIV 2007-404-2465) related to LGA s200; *Ballintoy Developments Limited and Another v Tauranga City Council* (CIV 2007-470-410) related to acceptance of payment of a specified amount.

between growth, asset and financial planning. In this respect, we have always seen one of the key advantages of contributions is the additional asset management planning effort that they encourage and the improved type and level of information that this makes available² about why costs are being incurred and the trade-offs that councils could choose to make. This ability is evolving, alongside improvements in asset and growth planning and reporting.

9. The point (p123) that growth-related infrastructure needs to be paid for (somehow) could receive greater prominence. Part of this is the long history of this type of development-related “contributions”, which in New Zealand dates back at least 130 years, and has been an important part of development of our towns and cities³. Over the medium-term, new infrastructure is essential to support growth while maintaining a liveable environment.
10. The nature of development contributions is that they reflect capital expenditure (not operating expenditure), and so it is appropriate that they are collected “up-front” (p 117). That is not to say that councils do not need to consider wider *financing* (as distinct from funding) issues such as the time over which expenditure is to be recovered, and the total costs that arise from that. Councils can model projected expenditure and revenue over time in setting their charges (as well as taking account of long-life assets).

The approach of collecting development contributions “over time” from new households is unlikely to be practical or desirable. Using illustrative figures of \$20,000 in contributions and annual rates of \$2000 indicates that rates (on new properties) would need to be approximately double for their first 13 years⁴ to provide equivalent funds to the council.

11. The report seems also based on the view that reduced contributions would lower house prices. While contributions are clearly a “development cost” housing prices are influenced by many factors, and it is unclear to what extent house prices would reduce if contributions were no longer charged.
12. The wider benefits of house ownership are also recognised. This includes the connection to social wellbeing (including effects of short-duration tenure that can be experienced by those renting). The “savings” (wealth) represented by owner-occupied housing is also important.

Reductions in the level of home ownership may be difficult to stop, and a range of issues are relevant to preserving social wellbeing in that scenario. These go far beyond the “price” of housing, and include the structure of housing providers and of the Residential Tenancies Act.

13. This submission refers generally to “housing” and “houses” for simplicity, however the wide range of dwelling types is also an important part of “housing affordability” and land use generally. The move towards larger houses is an important part of this.

² It is in our view unfortunate that the most recent LGA amendment introduced a requirement (LGA schedule 10, clause 3(2)) that expenditure related to several purposes (eg .renewal and growth) “must” be treated as if it were made for “the primary purpose”. This represents a reduction in the information being provided. An allowance that such expenditure “may” be so treated would be more appropriate.

³ The Plans of Towns Regulations Act 1875 provided for 1/10th of the land to be set aside as open space.

⁴ Assuming a simple 5% interest rate.

3 The proposal for “merit based appeals” for development contributions”

14. This section of the submission comments on the proposal (pp 126-127) that a “merit-based” tests be introduced for development contributions. It relates therefore to Questions 8.1 and 8.2. The merit-based test is outlined in the report with six points, reproduced below for convenience:

- a) *Is the project proposed justified either under the provisions of the RMA or by matters of substance and role?*
- b) *Has consideration been given to alternative funding methods and are there better options available?*
- c) *Do the charges pass the rational nexus tests, including reasonable provision for shares allocated to general rates (a rough proportionality test should be sufficient)?*
- d) *Are estimate of costs of supply and capacity life of asset reasonable (this is essentially an engineering assessment that might be satisfied by a commitment to competitive tender)?*
- e) *Does the calculation method have integrity?*
- f) *What are the implications of the fees and the way in which they are exacted for other community (and national) objectives and policies?*

15. We have significant concerns with such an approach and these points, as outlined in more detail below.

As a fundamental point, it must be recognised that development contributions are provided as one of a council’s funding tools (LGA s103). It is for the council to decide (via consultation with its community) on **what** it should spend money on; **how much** it should spend; and **how** the required funds should be raised. Councils make these decisions within the totality of the LGA and other legislation and after careful consideration of their obligations to all of their communities (LGA s10 and s14).

Allowing for external “review” of one part of those decisions needs to be approached very carefully. The development contributions policy (and other financial policies) are prepared, consulted on and adopted to “provide predictability and certainty about sources and levels of funding” (LGA s102). That requirement may be weakened if challenges can be made too readily.

Over the long-term that would reduce councils’ ability to go ahead with substantial growth-related projects. The Resource Management Act 1991 (**the RMA**) approach in particular made it difficult to fund long-term infrastructure needs related to incremental growth⁵.

16. *Point (a): Justification for the capital project*

We expect this refers to the set of capital projects that is part of each activity for which contributions are sought. We suggest that this point is already accommodated within council decision making, including the preparation of asset management plans and levels of service that identify how best to meet the adopted community outcomes. The operation of levels of service should also be improved through

⁵ It is expected that the Commission will be familiar with the timeline for the Rodney District Council plan change 62 (which introduced comprehensive funding for growth-related infrastructure via financial contributions).

initiatives associated with the recent changes to the LGA that introduced core activities, for which standard “performance measures” may be introduced (LGA ss261A-261F). Good asset management is a key part of operating development contributions.

It is important also to note that contributions will often only meet part of a project’s total costs (with the remainder funded through rates or another funding source).

17. *Point (b): Consideration of alternative funding methods*

This is the key point of LGA s101(3). Councils are obliged to, and do, consider the wide impacts of their funding decisions. In particular, this includes considering both causation and benefits.

The threshold for an external appeal to “second-guess” the authority of elected decision makers in this respect should be high. The current approach (via judicial review) provides that high threshold.

Any consideration of “better options” must be from the perspective of the community as a whole (which is the test already stated in s101(3)).

18. *Point (c): Rational nexus and proportionality*

This element could be advanced through best-practice guidelines (as commented on further below).

19. *Point (d): Costs of supply / capacity life / competitive pricing*

Councils are already committed to competitive procurement processes.

20. *Point (e): Integrity of calculation methodology*

This element could be advanced through best-practice guidelines (as commented on further below).

21. *Point (f): Implications for other objectives*

As noted above for point (b), this is a core part of local government decision-making around funding.

22. The “preference” from some parties for the appeal system that operated for financial contributions (under the RMA) is noted. That regime placed significant costs on to councils, and developers.

In relation to this, it is appropriate to note the following comments from the Quality Planning website (www.qp.org.nz):

FC [financial contributions] provisions in RMA plans are required to avoid, remedy or mitigate any potential adverse environmental effects generated by activities. They are also taken to provide for community facilities, such as reserves, and to provide for the increased demand placed on infrastructure. The taking of FCs for infrastructure does not always rest comfortably with the RMA as it is often based on fiscal rather than environmental considerations.

Attempts to fund 'growth' infrastructure have often floundered under the RMA due to:

- *high compliance costs in negotiation, mediation and litigation;*
- *considerable delay, and therefore poor responsiveness to changes in the social and economic environment;*

- *difficulty in establishing clear and quantifiable links between the environmental effects of a development and the amount of the financial contribution;*
- *decisions challenged and overturned by the Environment Court;*
- *piecemeal and slow development leading to fluctuating revenue streams; and*
- *as a consequence of the above, insufficient certainty for robust financial planning.*

DCs [development contributions] developed through the LTCCP process can only be challenged in the High Court on points of law and judicial review on process. Provisions under the RMA are subject to appeal to the Environment Court on merit as well as to the High Court on points of law and process.

DCs give LAs [local authorities] the scope to more effectively address the funding and provision of infrastructure; they also afford district plans and regional plans to deal with mitigating the environmental effects of development.

23. In conclusion, it is suggested that the introduction of “merit-based” appeals (as described in the report) would be a backwards and unnecessary step. The elements of this that have been proposed are already provided for in legislation, and could in some cases be strengthened through provision of best-practice guidelines.

The preparation and use of such guidelines should deliver similar benefits, without risking cutting across councils’ ability to make decisions for their communities, as required by the LGA.

4 Best practice guidelines

24. The proposal (p 124) that existing best practice guidelines for development be updated is supported. Councils, and developers, now have much greater experience with contributions.
25. It is possible that the process of updating the guidelines would also yield some principles that could then be reflected in legislative amendments (including to LGA schedule 13, which currently presents a very high-level approach to some of the key elements of setting contributions charges).
26. The guidelines need not be reflected in legislation to be effective (and ideally they should be well established before becoming part of statute). They could, for example, be a way for all stakeholders to communicate their views more clearly. They could also be used in external reviews⁶.
27. The guidelines could include:
- A standard terminology
 - A default approach (to any part of the policy) with departures noted for specific situations

⁶ The latest amendment to the LGA (the TAFM amendment) probably removed the DC policy and other similar policies from the LTP, and possibly therefore removed them from explicit audit (via Audit New Zealand as each council’s auditors). The legislation around this could be clarified although for many reasons this has little practical impact in any case.

- A standard way of setting out information (eg. for the capital programme)
28. In preparing any such guidelines, it will be important to keep in mind the overall approach and style of the LGA. The act generally provides principles and high-level direction, rather than detailed prescriptive requirements. While more detail might be appropriate for particular sections (including around development contributions as discussed here), any such moves must recognise the overall framework that they must operate in.

Performance measure reporting (LGA ss261A-) is an example of an area where consistency would be important (both to manage compliance costs and assist comprehension). Another area is the existing requirements in LGA schedule 10 for reporting of planned and expenditure.

29. With reference to consideration of economic efficiency, it is noted that development contributions principles established by several of the larger councils do make explicit reference to principles derived from economic analysis (including efficiency and equity)⁷.

5 Further comments particular parts of the report

30. Other jurisdictions (eg. Victoria, Australia) have provided for “standard” infrastructure charges that could be adopted by a council as a default charge (p 119). There may be merit in introducing such a system in New Zealand (though there may need to be more than one tier of charge, for example a “district”, “city” and “metro” level).
31. Minor amendments could be made to s8.4 to more accurately reflect the situation. The statement at the top of page 112 should make reference to use of s409 of the RMA being a transitional situation, and that the link there is to provisions of the Local Government Act 1974.

6 Conclusion

32. Thank you for the opportunity to make this submission. We would be happy to provide further clarification of any points we have made.

⁷ For example, refer to background methodology documents available from www.aucklandcity.govt.nz/developmentcontributions (accessed February 2012).