Property Council New Zealand

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Submission to Auckland Council on

Sharing the cost of Drury's growth – Contributions Policy 2022 variation A Consultation

8 November 2022

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Auckland Council 'Sharing the cost of Drury's growth – Contributions Policy 2022 variation A' consultation

1. Summary

1.1. Property Council New Zealand ("Property Council") welcomes the opportunity to submit to Auckland Council on the 'Sharing the cost of Drury's growth – Contributions Policy 2022 variation A' consultation ("DC Policy"). It is absolutely critical to have a robust Development Contribution ("DC") policy that would allow the industry to make informed long-term investment decisions and ensure fair distribution of the cost of development amongst all ratepayers.

1.2. Property Council strongly opposes the proposed increase in average development contribution fee per household from $22,564 to $83,251. This is an increase of over 268 per cent in the average development contribution fee per household. This increase is of an extreme magnitude and will have a significantly negative effect on the number of houses developed in Drury, will reduce housing affordability.

1.3. We are deeply concerned that Council intends to introduce a 30-year DC funding and financing model for Drury, because of the deep harm it will result in. Instead, Property Council recommends that the new Mayor and Council revises the proposed approach of the previous Council and replaces it with a 30-year strategic vision for Drury that is financed and funded in successive 10-year increments.

1.4. This would allow the Council to use alternative funding and financing mechanisms such as using the Crown Infrastructure Partners balance sheet through the Infrastructure Funding and Financing Act. Consequently, decreasing the rate of DCs in Drury down from an average of $83,251 and preventing unnecessary pressure on housing supply and affordability.

1.5. Property Council notes that 'causation' is not a term in the Local Government Act 2002. We are concerned that Council's proposal to incorporate causation in the DC Policy is unjustified. Accordingly, we recommend that the Council remove the causation component from the DC proposal. This would result in an immediate 9.5 per cent reduction in Drury DCs. We stress that we believe there needs to be greater reductions alongside those from removing causation.

1.6. Property Council is also deeply worried that this DC Policy will set a negative precedent for development across the rest of Auckland. In the event of similar changes to DCs in other areas, there is a high risk that future developments (residential, commercial, industrial and retail) currently in the pipeline will be put on hold. This is due to the significant impact of that changes to DCs of this scale entails. This will in turn put more pressure on Auckland's housing supply and will likely see the sector look outside of Auckland for development opportunities – only adding to New Zealand's housing affordability pressures.

1.7. A reduced development pipeline across Auckland will have a harmful effect on Auckland Council's finances, with reduced revenue from growth associated sources (both development contributions and future rates revenue).

2. Recommendations

2.1. We strongly oppose both the proposed 30-year funding model and over 268 per cent increase to DC fees for Drury. We have made a list of recommendations to influence better and fairer outcomes for all:

- The new Mayor and the Council does not adopt the 30-year infrastructure funding and financing approach due to a number of uncertainties (such as predicting the future cost of infrastructure and insurance) which could result in grossly overcharging through development contributions;
- The Council request officers to instead develop a 30-year strategic vision for Drury, with funding and financing occurring in 10-year increments;
- The Council request officers to develop a 10-year funding and financing plan that incorporates Crown Infrastructure Partners funding under the IFF;
- The Council remove causation from their modelling which would automatically decrease Drury DCs by 9.5 per cent (very much the minimum reduction PCNZ is seeking);
- The Council continue to work closely with developers that have already invested in infrastructure in Drury to ensure that double dipping does not occur; and
- The Council work closely with the private sector to better understand the implications that DC increases have on house prices.

3. Introduction

3.1. Property Council is the leading not-for-profit advocate for New Zealand's most significant industry, property. Our organisational purpose is, "Together, shaping cities where communities thrive".

3.2. The property sector shapes New Zealand's social, economic and environmental fabric. Property Council advocates for the creation and retention of a well-designed, functional and sustainable built environment, in order to contribute to the overall prosperity and well-being of New Zealand.

3.3. Property is Auckland's largest industry. Property provides a direct contribution to GDP of $12 billion (12 percent) and employment for 71,940 Auckland residents.

3.4. Property Council is the collective voice of the property industry. We connect property professionals and represent the interests of 387 Auckland based member companies across the private, public and charitable sectors.

4. Procedural transparency

4.1. The development sector remains deeply concerned with the lack of transparency from Auckland Council regarding Drury development contributions. When Auckland Council previously consulted on Drury development contributions in 2021, Property Council raised our concerns that the formal consultation period on Drury development contributions lasted less than one month, was during a COVID-19 lockdown, and did not make Council modelling available to the public.

4.2. As a result, the previous Council delayed the implementation of new DC fees in Drury, with instructions to provide the public with more information, but still committed to a 30-year funding timeframe, in principle, for other Investment Priority Areas.

4.3. We firmly believe that the previous Council made an error in agreeing to an in principle 30-year funding and financing timeframe approach without having clarity on what the modelling or costs would be on future development.

4.4. The current consultation process has similarities with the 2021 process. We once again have had limited time and data provided (requiring the use of the Official Information Act by Property Council), with the most recent data being provided 13 working days before the due date of this submission. We understand that the root cause of difficulties and uncertainty that have arisen throughout the Council's process – is because of the 30-year funding timeframe ideology.

4.5. Despite having the late additional data, one clear question remains a concern from our members – how capital expenditure be accurately calculated and allocated beyond a 10-year period? This question remains unanswered by Council staff, due to the complexities that a 30-year timeframe establishes.

4.6. In particular, we have been advised by Council staff that if DCs are over-collected, at the end of the 30-year period the Council will track down developers to provide compensation. This proposal is very far from ideal. We are not aware of this happening at present, where Auckland Council proactively refunds overpaid development contributions. Anecdotally, the property sectors experience to date has been the opposite.

5. 30-year timeframe creates complexities with funding and financing

5.1. The previous Council worked towards introducing a 30-year timeframe to fund and finance infrastructure in Drury, using development contributions. This is a significant change from current 10-year timeframes within Long Term Plans.

5.2. It is essential that Auckland Council has a robust DC policy that allows developers to make informed long-term investment decisions and ensures a fair distribution of fees amongst all ratepayers. However, when looking at the cost of infrastructure over a 30-year timeframe, complexities arise around the accuracy of the price of infrastructure creating uncertainty. Particularly, when trying to estimate things such as inflation, delivery risks, costs of infrastructure, and future infrastructure demand over a 30-year period.

5.3. Under section 197AA of the Local Government Act, Auckland Council must ensure that a 30-year approach is fair, equitable and is proportionate of the total costs of capital expenditure to service growth over the long term. We have serious concerns that the calculations become increasingly inaccurate and uncertain past 10 years.

5.4. Furthermore, there are a number of things that add to the complexity of the modelling and will need to be considered by Council such as:

- Impact of inflation on delivery of projects over time;

- Benefits of paying upfront vs. delivery risks;
- The accuracy of capital expenditure allocations that far in advance, given that each development will not necessarily generate the same demand on infrastructure;
- Evidence supporting the Council's intent to take a 30-year approach;
- Actions the Council will have to take to ensure money collected today will be spent on delivery of the projects over 30-year period;
- The impacts on development in the short term;
- Lack of evidence suggesting that a 30-year approach is better than a 10-year one; and
- The time value of money, and how the real value of contributions collected today will not erode through inflation, specifically in relation to the increasing costs of the anticipated future infrastructure against which it is allocated.

5.5. The proposed changes lack transparency and raise concerns around the accuracy of the proposed DC charges. For example, things like the impact of inflation are extremely difficult to predict over a 30-year timeframe. We have real concerns that there could be over collection of DCs in which the Council will be legally required in 30-years' time to track down the developers and return amount of overcharge. This will add layers of complexity for the Council and is another reason why we support 10-year funding and financing timeframes, supported by a 30-year strategic vision, over the current 30-years funding model.

5.6. Property Council is also concerned that the Council has not demonstrated sufficient consideration of alternative funding methods such as Infrastructure Funding and Financing through the Crown Infrastructure Partners. Both Wellington City Council and Tauranga City Council are using Crown Infrastructure Partners to fund significant infrastructure projects within their region.

5.7. The Infrastructure Funding and Financing Act was introduced by the government in recognition that existing development contributions mechanisms have been unsuccessful in appropriately allocating growth costs and have already been successfully utilised in Auckland for greenfield development in Milldale and are implemented internationally.

5.8. The main difference between DCs and the Infrastructure Funding and Financing Act, is the level of certainty of over costs. For example, to apply for funding support from the Crown Infrastructure Partners, more certainty of actual costs is required. In comparison, DCs are a blunt tool that allow Council's to be less accurate with the numbers and costs. It is disappointing to see that Auckland Council has once again chosen to use the blunt tool that is DCs which will result in the Council missing out on the opportunity to have Crown Infrastructure Partners funding and to reduce the impact of DCs on housing supply and affordability.

5.9. We recommend the new Mayor and the Council not adopt the 30-year infrastructure funding and financing due to a number of uncertainties (such as predicting the future cost of infrastructure and insurance) which could result in grossly overcharging through development contributions. We already have many questions relating to the proposed cost of infrastructure, as we believe the costs are overstated as discussed later in our submission.

5.10. Instead, we are supportive of a 30-year strategic vision for Drury, with funding in 10-year increments that can be reforecast overtime. This would better ensure that project costs are greater aligned to upcoming projects and lowers the risk of cost blow-outs from insurance or overcharging through DCs. Reforecasting every 10 years will also allow for alternative funding and financing mechanisms through the Infrastructure Funding and Financing Act and reduce the proposal to have a $83,000 average DC fee per household. This will help ensure fairer allocation, better transparency and intergenerational equity.

6. Problems with the model

Causation

6.1. The causal nexus test was established in New Zealand case law.[1] The causal nexus test determines whether development contributions are paying for infrastructure needed as a consequence of growth. If the development contributions are not, there is no causal nexus, therefore developments are an inappropriate funding mechanism.

6.2. The purpose of development contributions should be to fund growth induced demand for core infrastructure, such as transport or three waters, that is crucial to the viability of a given development. Our members support this premise of development contributions and are in favour of paying an equitable share of the cost of additional core infrastructure.

6.3. Problems arise when councils treat development contributions as an alternative funding mechanism to increasing rates for services and infrastructure that may or may not be used by the eventual users of those developments.

6.4. For example, the Council's model estimates benefits based on household numbers – i.e., use of a facility or asset. The model then <u>adds</u> a causation component – i.e., if the asset was purchased to cater for growth needs, then 100% causation to growth. We disagree with this connection. Using causation to load cost onto growth is problematic and extremely tenuous.

6.5. We therefore strongly disagree with the Council including causation into their modelling. 'Causation' is not a term found in the Local Government Act 2002. If the Council remove causation from their modelling this would see a reduction of $44m or 9.5 per cent of costs. The Council incorporating causation into their modelling is a blunt and disingenuous way to collect more fees.

6.6. We are concerned that without ringfencing DCs to the Drury development, removing causation and reforecasting infrastructure every ten years, there will be significant equity issues. It is extremely problematic that a household moving into the Drury development in the early years, will contribute to the upfront cost of thirty years' worth of infrastructure, the benefit of which they may never see or experience in their time living in Drury. Furthermore, given the difficulties in modelling infrastructure demand over a thirty-year timeframe, it is possible that some of the pre-paid infrastructure could not be required in the future and thus, will not be built. This does not seem equitable or fair.

[1] *Neil Construction Limited & Ors v North Shore City Council 2007*

6.7. We recommend the Council remove causation from their modelling which would decrease Drury DCs by 9.5 per cent. Despite our request to remove causation and decrease DCs by 9.5 per cent, it is important for the Council to recognise that the overall percentage increase is still extremely significant even if causation is removed. This remains an unacceptable burden on the sector, and we strongly recommend further reductions.

Prices may not affect actual costs and in some cases are introduced 'after the fact'

6.8. We have concerns that the current prices of infrastructure are inflated and do not reflect actual costs. Not only do we have concerns with current pricing, but our concerns exponentially increase beyond the 10 year forecast due to the uncertainty of pricing increasing.

6.9. We are also concerned about the potential for double dipping. In particular, where private developers have paid for a piece of infrastructure (i.e., stormwater) but are being charged for that same piece of infrastructure through development contributions. We strongly recommend that the Council continue to work closely with developers that have already invested in infrastructure in Drury to ensure that double dipping does not occur, due to the serious nature of consequences if discovered.

6.10. Another concern we have relates to land costs. In 2018, Hamilton City Council commissioned Insight Economics[2] to complete an independent report on the likely developer reactions to increased DC charges. The report signalled a number of issues with DCs, which align with our concerns. In particular:

> "**As DCs increase, the cost of land development rise, and thus its profitability falls**…In other words, land developers (who physically pay the DC) will seek to share some of the cost with raw land owners by paying them less for their land…it is unlikely that the resulting fall in land prices will be sufficient to fully compensate them. **As a result, the increase in DCs will also increase the total cost of land development**…"
>
> "**In summary,** economic theory predicts that the imposition of **higher DCs will impact most, if not all, participants in the wider property market."**

6.11. We are particularly concerned that DC costs are rising after land is sold. Thus, the above example where land developers will seek to share some of the cost with raw landowners cannot occur after the fact. More alarmingly, in some instances contracts for residential development have already been negotiated and signed, long prior to the Council proposing a significant increase in DCs. Thus, higher DCs will impact more significantly on developers and future residents having to share the load of DCs.

6.12. Given the above, we recommend the Council consider removing causation within their model to reduce costs automatically and at minimum by 9.5 per cent. We would also like to see reforecasting every 10-years to unlock Crown Infrastructure Partners funding as stated earlier in our submission. We believe that these recommendations would improve intergenerational equity and ensure that

[2] Insight Economics. (2018). Likely Developer Reactions to Increased Development Contribution Charges. Retrieved from https://www.hamilton.govt.nz/our-council/10-year-plan/10Year%20Plan%20documents/Economic%20report%20-%20Likely%20Developer%20Reactions%20to%20Increased%20Development%20Contributions%20Charges%20-%20Insight%20Economics%20Ltd.pdf

those who benefit from the community infrastructure help contribute towards it over a longer period of time, reducing the financial burden upfront (i.e., within house prices).

7. Housing Affordability

7.1. Direction 3 of the Auckland Plan seeks to shift to a housing system that "ensures secure and affordable homes for all". The proposed Drury DC Policy will result in diametrically opposed outcomes.

7.2. Increased DC fees in Drury will likely result in the following outcomes:

- Additional costs being passed on to the eventual buyer or occupier, making housing and occupancy costs more expensive; and/or
- Planned developments are postponed or cancelled, due to increased costs reducing the overall affordability of the development or project;
- Less affordable typologies of housing being built.

7.3. The Council economist has stated that it does not consider these increases will impact housing affordability. We disagree. Property Council's 2021 Economics Assessment[3] concluded that the changes will reduce supply, increasing prices for existing stock and passing on the DC increases into the price of new housing stock (in cases where developers are not entirely deterred from constructing more housing).

7.4. Additionally, Property Council New Zealand has established a Development Contributions Members Taskforce consisting of 45 member companies across the Auckland region. The Taskforce was established in the past month out of concern for the proposal to significantly increase DC fees in Drury and potentially in other Investment Priority Areas across Auckland. Our members concern came from their own practical experience that increased DC fees are often put onto the eventual buyer or that projects are delayed and/or cancelled due to feasibility issues.

7.5. Adding to our affordable housing concerns are the Council's predictions for the price of land in Drury. For example, the Council have priced Drury land at the equivalent price of St Heliers. Given the greater distance of Drury from the CBD, and geographic impediments on development, we struggle to see the parallel. The difficulty of predicting land prices over the 30-year period is significant and the Council's predicted land price in Drury is not conducive to predicted values in the coming years.

7.6. Furthermore, accumulative costs are an important factor in DC considerations. Our Auckland industry members are already facing huge inflationary costs across the board. In particular, construction costs have gone up between 5-15 per cent, land values have increased between 20-30 per cent, while building material costs have gone up by 5-15 per cent in the last year alone.[4] These increases have to be factored into the DC policy.

7.7. It's easy to look at one proposed change and expect that it will have minimal impact, but collectively these reforms could significantly increase the cost and risk of development. At a time when we

3 Economics Assessment, pages 8 and 9

4 Consumers set to pay, as builders have a supply chain reaction. Stuff NZ. 9 July 2021. Retrieved from https://www.stuff.co.nz/business/125690062/consumers-set-to-pay-as-builders-have-a-supply-chain-reaction

desperately need to be increasing our housing supply, particularly of affordable housing, and streamlining development, we are potentially creating a 'perfect storm' that could have the opposite effect.

7.8. We have serious reservations towards the Council believing that increasing DCs will not result in house prices increasing. Increasing DCs by over 268 per cent will have significant consequences and likely hinder unlocking Drury development altogether.

8. Impact on Auckland Council Finances

8.1. Auckland Council is currently facing significant budgetary pressure, as a result of factors such as high inflation. The latest Auckland Council estimate is for a $270 million budget shortfall in the 2023/2024 financial year[5].

8.2. Property Council notes our firm belief that the proposed approach to Drury development contributions will likely deter already planned development, both in Drury and other Investment Priority Areas. This will have a direct impact on Auckland Council's rating base and the ability to allocate Auckland City's budget across a larger pool of rate payers in future years. Deterring development in growth areas through unpredictability will reduce increased income associated with growth, in terms of both development contributions and future rates revenue.

8.3. As such, we once again strongly urge Auckland Council to reconsider the proposed 30-year approach to Drury development contributions (along with other Investment Priority Areas).

9. Conclusion

9.1. The DC regime for Auckland is significant interest to our Auckland based members. In order for the property sector to make informed long-term investment decisions, it is vital to ensure fair distribution of fees amongst all ratepayers while not creating a further barrier to the development of affordable housing.

9.2. The proposed approach to DCs in Drury is deeply flawed and Property Council strongly opposes it. We are deeply concerned that the proposed policy will establish a precedent that will restrict much needed development across broad swathes of Auckland, resulting in flow on effects to housing affordability and supply.

9.3. To mitigate our concerns, we recommend the following:

- The new Mayor and the Council does not adopt the 30-year infrastructure funding and financing due to a number of uncertainties (such as predicting the future cost of infrastructure and insurance) which could result in grossly overcharging through development contributions;
- The Council request officers to develop a 30-year strategic vision for Drury, with funding and financing occurring in 10-year increments;
- The Council request officers to develop a 10-year funding and financing plan that incorporates Crown Infrastructure Partners funding under the IFF;

[5] Auckland Council Budget Update. Auckland Council. 07 November 2022. Retrieved from: https://ourauckland.aucklandcouncil.govt.nz/news/2022/11/auckland-council-budget-update/

- The Council remove causation from their modelling which would automatically decrease Drury DCs by 9.5 per cent (very much the minimum reduction PCNZ is seeking);
- The Council continue to work closely with developers that have already invested in infrastructure in Drury to ensure that double dipping does not occur; and
- The Council work closely with the private sector to better understand the implications that DC increases have on house prices

9.4. We wish to be heard in person in support of our submission, should there be an occasion provided by the Council. For any further enquiries, please do not hesitate to contact Logan Rainey, Advocacy Advisor, via email: Logan@propertynz.co.nz or cell: 021410787.

Yours sincerely,

Andrew Hay
Auckland Regional Chair
Property Council New Zealand