Master Builders Australia

Infrastructure Costs

January 2014

MASTER BUILDERS
AUSTRALIA

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1 Introduction

1.1 Master Builders Australia is the nation's peak building and construction industry association which was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder state and territory Associations. Over 122 years the movement has grown to 32,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three sectors, residential, commercial and engineering construction.

1.2 The building and construction industry is a major driver of the Australian economy and makes a major contribution to the generation of wealth and the welfare of the community, particularly through the provision of shelter. At the same time, the wellbeing of the building and construction industry is closely linked to the general state of the domestic economy.

2 Overview

2.1 Australia faces a major infrastructure challenge over coming decades, both in the maintenance and the remediation of existing infrastructure assets, and investing strategically in expanding our infrastructure base.

2.2 As a nation, Australia has an enormous, and growing, infrastructure shortfall, which is undermining our national productivity performance and that of key industries and sectors.

2.3 The current review being undertaken by the Productivity Commission is welcome if it highlights the nature, consequences and offers bold policy reforms to ameliorate this shortfall.

2.4 A rigorous, analytical report, while useful, must be carried forward by decisive action by governments - Federal, State and Local - with an active and suitable role for the private sector.

2.5 Expanded and more efficient infrastructure supply is likely to deliver a number of important benefits, most notably:

- encourage increased investment, and through this employment;

- lower costs of construction for residential housing and non-residential construction; and,
- increased productivity, with flow on benefits throughout the economy.

2.6 While increasing our infrastructure productivity will require action across a number of policy domains, an essential element must be meaningful labour market reforms, focusing on reinforcing the rule of law in critical sectors of the building and construction industry as a means of reducing construction costs and lifting labour productivity.

2.7 Redressing the infrastructure shortfall will also require action on both public and private sector funding of key economic and social infrastructure, through inter alia:

- lifting direct public sector spending on key infrastructure to at least 6 per cent of GDP by 2020; and,
- facilitating greater engagement by private sector investors in suitable infrastructure arrangements and platforms.

2.8 It will also mean further decisive action to remedy shortcomings in the way urban infrastructure is funded and delivered.

3 Terms of Reference

3.1 The Federal Government formally announced on 13 November 2013 an inquiry into infrastructure costs, to be undertaken by the Productivity Commission (Abbott, Hockey and Briggs, 2013; Hockey, 2013b).

3.2 In commissioning the review, the Federal Government observed:

- efficient public infrastructure has a vital role to play in facilitating a competitive and productive economy;
- ongoing financing and funding of infrastructure development is of critical importance to Australia's economic future;
- the capacity of governments to adequately fund new and improved infrastructure is limited; and,

- in the future, there will be a greater need to rely on private sector financing of infrastructure supply.

3.3 Under its terms of reference, the inquiry is examine:

- ways to encourage private sector financing and funding for major infrastructure projects; and,
- issues relating to the high costs and long lead times associated with such projects.

3.4 Key elements of the review include to:

- examine costs, competitiveness and productivity in the provision of nationally significant economic infrastructure;
- identify ways to reduce infrastructure construction costs;
- address barriers to private sector financing, including examining the role and efficacy of alternative infrastructure financing and funding mechanisms;
- recommend mechanisms and operating principles that could be applied to overcome these barriers; and,
- outline any other options the Productivity Commission might identify to reduce construction costs.

4 Linkages

4.1 The building and construction industry is an enabling industry; it is one of the most 'linked-in' to other industries within the Australian economy.

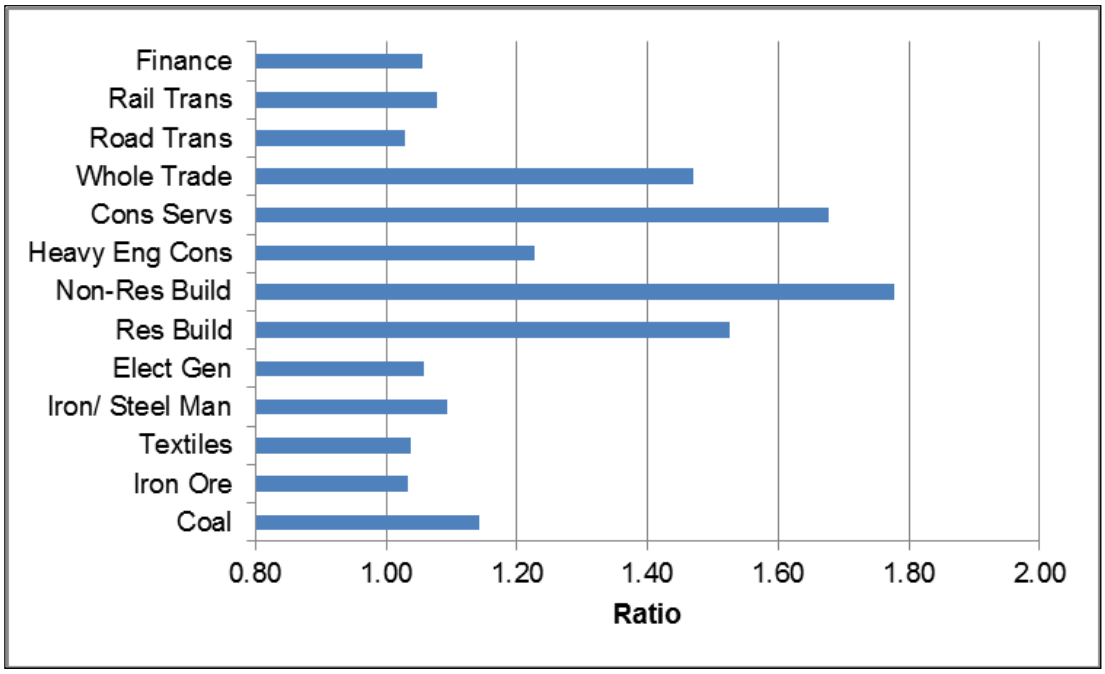
4.2 The output of the building and construction industry is one of the most used by, and is one of the largest commercial and industrial users of the outputs of, other industries within the Australian economy.

4.3 Adapting a measure of industry specialisation produced by the Australian Bureau of Statistics (ABS 2013b), Master Builders has developed an integration ratio which measures the degree to which the inputs to/outputs of an industry come from/go to other industries.

4.4 A higher measure of integration (the further it is above 1.0), the more integrated that industry/sector is with other industries/sectors.

4.5 As Graph 1 highlights, key sectors of the building and construction industry, namely residential building construction, non-residential building construction, heavy and civil engineering construction, and construction services are amongst the most closely integrated with other Australian industries.

Graph 1: Building Industry Integration with Other Industries



4.6 Non-residential building and construction is the most highly integrated-with-other-industries sector in Australia, with an integration ratio of 1.78, following by construction services at 1.68, residential building at 1.53, and heavy and civil engineering at 1.23.

4.6.1 The only other industries with similar integration ratios are wholesale trade (ratio = 1.47), and accommodation and retail trade (each at 1.39).

4.7 The stand-out integration ratios for the main sectors of the building and construction industry sends a very clear and simple message:

- what happens to the costs and the productivity of the building and construction industry has important implications for other industries, and the Australian economy.

- Looked at another way, major reforms in the building and construction industry, such as those relating to infrastructure costs and supply, and the labour market are likely to have major spill-over benefits for other industries, and the Australian economy.

5 Infrastructure and Housing

5.1 The infrastructure-housing nexis is clear and strong: inefficient and/or inadequate infrastructure adds to the cost of housing.

5.1.1 This linkage is particularly important between transport and housing, as the great bulk of Australians need to travel each day between their homes, and their schools, workplaces or other essential places of mainstream life.

5.1.2 Poor transport infrastructure - whether roads, bridges, rail or ferry systems - for example, only serve to push housing prices higher than they would be otherwise.

5.2 As the Deputy Governor of the Reserve Bank of Australia (Lowe, 2013) observed:

> *"… investment in transportation infrastructure - by making it easier to move around the city - can increase the supply of 'well located' land. And when supply increases, prices adjust. This means that underinvestment in transportation networks tends to put upward pressure on housing costs."*

5.3 Econometric modelling by the Reserve Bank of Australia (Kullish et al, 2011) examined two different infrastructure scenarios:

- the first being where there had been significant investment in transport infrastructure (the 'high investment' scenario); and,
- the second where there had been much lesser investment in transport infrastructure (the 'under-investment' scenario), resulting in higher-than-otherwise transport costs.

5.4 Amongst the key findings from the modelling of the 'under-investment' scenario were:

- commuting was more costly;

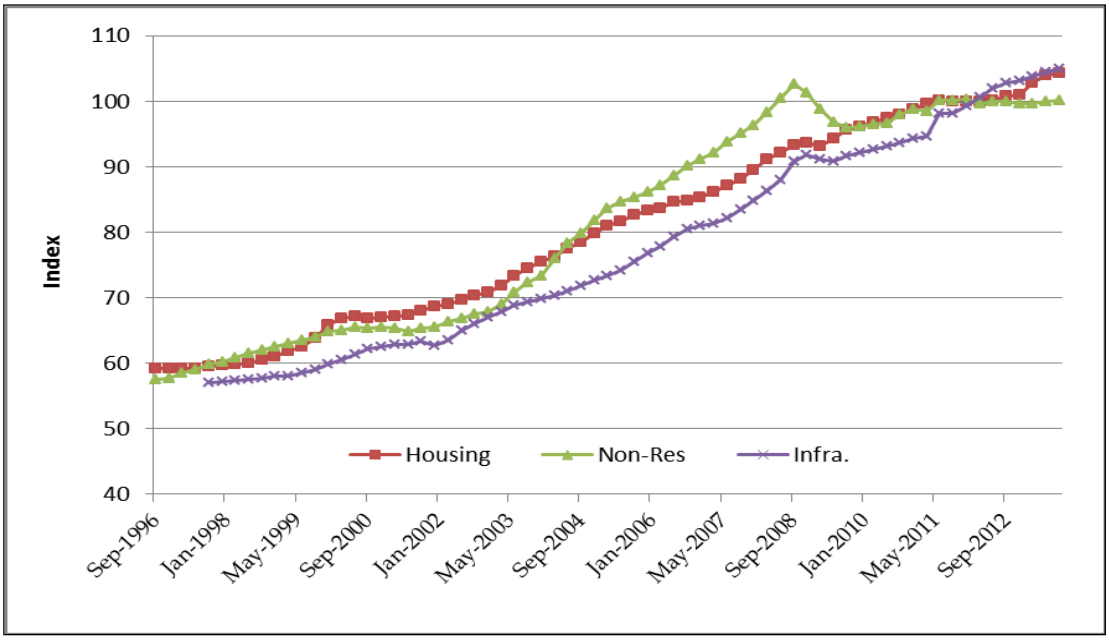
- household sizes (measured in terms of floor area per square metre, rather than the number of persons) are smaller than otherwise;
- population densities were much higher, and more concentrated, around city centres;
- house and land prices were much higher in areas closer to city centres, and lower in the city fringes; and,
- with these distance effects being strongest in Sydney, Melbourne and Adelaide, more so than Brisbane or Perth.

5.5 Taken as a whole, the modellers-report's authors concluded (Kullish, 2011: 9):

> "*Overall, the effect of poor transport infrastructure and higher transport costs is that households spend more of their resources commuting, live in smaller houses and face higher average housing and land prices."*
>
> *"By contrast … well-directed investment in transport infrastructure makes it more feasible to live further from the CBD (central business district) and can thereby reduce the cost of housing."*

5.6 The linkages between infrastructure and housing can also be seen in the strong relationship between the output prices of each the sub-sectors of the building and construction industry, which have shown a more or less consistent pattern of increase over the period 1996 - 2013, as can be seen in Graph 2.

Graph 2: Output Prices in the Building and Construction Industry



5.7 While output prices in the non-residential construction sector dipped in late 2008 and have shown little growth in the period since, those for new residential dwellings and infrastructure[1] have continued to so on an upward trend.

5.8 Not surprisingly, there were very strong practical and statistically significant relationships between each of the pairs of output price series[2] , between:

- infrastructure and new dwelling output prices: r = 0.991; t = 58.48; p = 0.00;
- infrastructure and non-residential building output prices: r = 0.960; t = 27.34; p = 0.00; and,
- new dwelling and non-residential building output prices: r = 0.977; t = 36.47; p = 0.00).

[1] Proxied from the 'roads and bridges' data series published by the ABS (2013a)

[2] For the general reader: r is a measure of association, also known as practical significance; while t and p are measures of statistical significance, in particular the likelihood the results are due to chance alone.

5.9 The very strong practical and statistical significance for the correlations suggest an exceptionally high degree of commonality amongst the output prices of the three sub-sectors under consideration. This assessment is confirmed by a Principal Components Analysis (PCA), which found for:

- the first Principal Component: Eigenvalue = 2.95; Proportion = 0.984; and,
- the second Principal Component: Eigenvalue = 0.04; Proportion = 0.014.

5.10 Taken together, these results (both for the correlation and the PCA) would suggest there are some strong common elements of output prices for new dwelling construction, non-residential construction, and infrastructure, which in turn implies any economic and/or other public policy reforms focusing on infrastructure (as per the terms of reference for the current PC inquiry) may well have substantial and positive spill-over effects for new dwelling and non-residential construction.

5.11 Correlation is, however, not causation; it is just a measure of the coincidence of the variables under review. Nor does it speak to the more important question of 'which causes which'?

5.12 Given the importance of infrastructure for home-owners (as consumers of new dwellings) and for commerce and industry (as consumers of non-residential construction), rather than the other way around, causality is more likely to run from infrastructure to new dwelling/ non-residential construction, than the other way around.

5.13 Two simple, first-look, models illustrate the potential impact of infrastructure reform on both the dwelling and the non-residential construction sectors.

5.13.1 The first model examines the impact of output prices in the infrastructure sector on those in the residential dwelling construction sector - the impact of the cost of infrastructure on the cost of housing.

5.13.2 The second model looks at the impact of output prices in the infrastructure sector on those in the non-residential construction sector - the impact of the cost of infrastructure on the cost of schools, hospitals, shops, offices and the like.

5.14 Both models are estimated in 'double-log' form (meaning the results should be seen as elasticities) for ease of interpretation, comparison and analysis within and across the two models.

5.15 In the models, the mnemonics (code names) are as follows:

- lhouse = log of the producer prices for dwellings;
- lnonres = log of the producer prices of non-residential construction;
- linfra = log of producer prices of infrastructure;
- trend = a dummy variable for measuring any underlying time trend; and,
- C = constant (a standard characteristic of econometric modelling)

5.16 Residential Building

5.16.1 Table 1 reports the impact of infrastructure pricing on house prices.

Table 1: Impact of Infrastructure Pricing on House Prices

Dep Var = LHOUSE			
Variable	**b**	**t**	**p**
C	2.65	4.76	0.00
LINFRA	0.35	2.48	0.02
TREND	0.01	3.85	0.00
R Sq	0.987		
Adj R Sq	0.987		
Log Like	161.62		
F-Stat	2395.67		
P (F-Stat)	0.000		

Source: Master Builders Australia

5.16.2 The key message from this modelling is: infrastructure prices have a substantial practical and powerful statistically significant impact on dwelling prices.

5.16.3 A one per cent increase in infrastructure prices can be expected to increase house prices by 0.35 per cent in the short term, and this result is most unlikely to be due to chance alone (t = 2.48; p = 0.02).

5.16.4 The model also reports strong explanatory power and very good diagnostics.

5.17 Non-Residential Building

5.17.1 Table 2 reports the impact of infrastructure pricing on non-residential construction prices.

Table 2: Impact of Infrastructure Pricing on

Non-Residential Construction Prices

Dep Var = LNONRES			
Variable	**b**	**t**	**P**
C	-2.24	-1.79	0.08
LINFRA	1.59	5.02	0.00
TREND	-0.01	-2.08	0.04
R Sq	0.944		
Adj R Sq	0.942		
Log Like	109.10		
F-Stat	521.32		
P (F-Stat)	0.000		

Source: Master Builders Australia

5.17.2 Infrastructure pricing appears to have a much greater impact on non-residential (that is, commercial) construction prices than it does on dwelling prices, by a factor of around 4 times.

5.17.2.1 A one per cent increase in infrastructure prices can be expected to increase non-residential construction prices by 1.57 per cent in the short term, and this result is highly unlikely to be due to chance alone (t = 5.02; p = 0.00).

5.17.3 The model also reports strong explanatory power and very good diagnostics.

5.17.4 Taken together these two simple models illustrate an important point:

- rising infrastructure costs add to the costs of both residential and non-residential construction,

5.17.5 The corollary of which is meaningful reforms which deliver noticeable and sustained reduction in infrastructure supply costs are likely to be reflected in lower costs of residential and non-residential construction.

5.17.5.1 That is, lower cost houses, apartments, schools, hospitals, offices and shopping centres.

5.17.5.2 Quite simply, a lower cost of living for Australian families.

6 Reform – Workplace Relations

6.1 The building industry needs a productive workplace relations environment. Harmonious and productive workplaces are vital to a strong building industry, a thriving economy and increasing employment opportunities. Sadly, building and construction industry unions have a long history of militant and often unlawful behaviour, particularly wildcat strike activities that disrupt workplaces.

6.2 Such irresponsible behaviour lowers productivity and adds to the cost of building much needed economic and social infrastructure, such as hospitals and schools - which are funded by taxpayers. The building industry requires an additional 300,000 workers, independent contractors and apprentices over the next decade to meet projected demand and offset employees entering retirement. However, the current system discourages many building and construction firms, especially small contractors, from hiring more workers and training more apprentices.

6.3 To address these challenges, Australia must return to a balanced and fair

relations system; one that can be easily understood and is easy to comply with.

6.4 The restoration of a strong and effective the Australian Building and Construction Commission (ABCC) will prove invaluable for increasing productivity in commercial building, infrastructure supply and the economy in general. As Master Builders' observed (Harnisch, 2013b), when the Federal Government introduced the Building and Construction Industry (Consequential and Transitional Provisions) and the (Improving Productivity) Bills 2013 into the Federal Parliament on 14 November 2013, the legislation:

> *"will see the return of the regulatory agency capable of tackling head on industrial thuggery, boosting productivity in the (building and construction) industry and lowering the costs of construction to the benefit of taxpayers."; and further,*
>
> *"By reforming the industrial relations culture of the industry and ensuring building union members behave as normal members of the community, the return of the ABCC will be an important (factor) in driving economic growth and jobs."*

6.5 Master Builders has comprehensively identified changes to the Fair Work system that would enhance productivity[3].

6.5.1 These are vital reforms especially in relation to greenfields agreements where the problems isolated in Attachment A are causing detriment to the economy.

6.6 The importance of labour market reform, in particular the return of the rule of law into key sectors of the building and construction industry, is highlighted in a report by Independent Economics (IE, 2013), commissioned by Master Builders Australia. The report examines and models the impact of key changes to labour laws impacting the building and construction industry on productivity in the industry, and in key macroeconomic indicators.

6.7 The labour laws considered were the:

[3] Master Builders' paper entitled *"Essential Changes to the Fair Work Act Regime"* is at Attachment A.

- creation and operation of the Australian Building and Construction Commission (ABCC; between 2002 and the middle of 2012 - the 'ABCC era'); and,

- termination of the ABCC, and its replacement by the Fair Work Building Inspectorate (also known as Fair Work Building and Construction; FWBC), which has been in operation since the middle of 2012 (the 'FWBC era').

6.8 The econometric modelling identifies four sectors within the building and construction industry, namely residential building, non-residential construction, engineering construction (which can broadly be taken as a proxy for 'infrastructure') and construction trade services.

6.9 The Independent Economics report made a number of observations about the productivity performance of the building and construction industry during the ABCC period:

- labour productivity in the building and construction industry out-performed that of other industries by 21.1 per cent during the ABCC period;

- multifactor productivity in the building and construction industry surged by 16.8 per cent in the decade to 2011/12;

- total factor productivity in the building and construction industry grew by 13.2 per cent between 2003 and 2007, well ahead of the 1.4 per cent recorded between 1998 and 2002;

- the ABCC likely added 9.4 per cent to productivity in the building and construction during its years of operation; and,

- three-quarters (75 per cent) of this gain is likely to be lost because of the labour law changes associated with the abolition of the ABCC its replacement with the FWBC.

6.10 The modelling undertaken by Independent Economics (IE, 2013) looked at the macroeconomic impacts, and the effects on the building and construction industry of the:

- operation of the ABCC (the 'ABCC era'); and,

- abolition of the ABCC and its replacement by the FWBC (the 'FWBC era').

6.11 The introduction and the operation of the ABCC was found to have generally delivered higher labour productivity and lower construction costs.

6.12 In macro-economic terms, the ABCC:

- increased real consumption by 0.9 per cent;
- increased real consumer wages by 0.3 per cent;
- increased gross domestic product by 0.9 per cent; and,
- lifted household welfare by $7.5 billion (in 2012/13 dollar terms).

6.13 For the building and construction industry, the ABCC:

- lowered the costs of construction by 3.6 per cent for engineering building construction;
- lifted investment in buildings and structures by 2.7 per cent;
- reduced the costs of buildings and structures by 3.4 per cent; and,
- increased real value added in the engineering building construction sector by 3.6 per cent.

6.14 By contrast, the abolition of the ABCC and its replacement with the FWBC resulted in a loss of productivity and higher construction costs.

6.15 In macro-economic terms, replacing the ABCC with the FWBC has meant, inter alia, a:

- reduction in real consumption by 0.7 per cent;
- reduction in real consumer wages by 0.2 per cent;
- reduction in gross domestic product by 0.6 per cent; and,
- decline in household welfare of $5.5 billion (in 2012/13 dollar terms).

6.16 For the building and construction industry, it meant:

- increasing the costs of construction by 2.7 per cent for engineering building construction;
- reducing investment in buildings and structures by 1.9 per cent;
- lifting the costs of building and structures by 2.6 per cent; and,
- reducing real value added in the engineering building construction sector by 2.5 per cent.

7 Funding – Public Sector

7.1 An efficient and high-quality infrastructure base is vital to Australia's productivity and international competitiveness, and our sustained economic growth and development. Without capacity-enhancing investment in infrastructure, both by the public and the private sectors, Australia's economic performance with stagnate and living standards will decline.

7.2 Inadequate public sector investment in infrastructure by successive Federal, State/Territory and Local Governments in the past is being manifest in

- worsening bottlenecks, inadequate urban infrastructure (both in capital cities and in major regional areas), and
- ailing services in our hospitals, schools and other social infrastructure.

7.3 These pressures will only compound as Australia's population grows, from around 22 million in 2010, to 26 million in 2020, and then more than 30 million by 2030 - an increase of more than 32 per cent in just 20 years.

7.4 Australia faces a major infrastructure challenge over coming decades, both in the maintenance and the remediation of existing infrastructure assets, and investing strategically in expanding our infrastructure base. The Federal Government's own infrastructure advisory agency (Infrastructure Australia, 2013: 6) has estimated Australia's national "infrastructure deficit" to be around $300 billion.

7.5 Private sector estimates (BCA, 2013: 3) suggest as a nation we will need to spend at least $760 billion on infrastructure over the next 10 years just to stop us sliding backwards.

7.6 The public sector has for many years failed to adequately finance Australia's core infrastructure needs and appears even less likely to be able to do so in the future, pointing toward an even greater role for the private sector in infrastructure supply.

7.7 Public sector spending on infrastructure, at around 3 to 4 per cent of gross domestic product (GDP), has been inadequate to supply key economic and social infrastructure, and should be lifted progressively to at least 6 per cent of GDP by 2020.

7.8 Federal, State/ Territory and Local Governments need to, inter alia:

- redirect spending away from recurrent and less productive expenditures, toward investing in efficiency- and competitiveness- enhancing infrastructure;
- improve policy co-ordination within, and across, the various tiers of government, with the Council of Australian Governments (COAG) taking the lead in developing an integrated plan for Australia's economic and social infrastructure needs; and,
- remove impediments, such as unfavourable capital-raising, regulatory, taxation regimes, to greater private sector investment in infrastructure.

7.9 Key elements of a robust reform agenda which are properly the function of the government/ public sector should include:

- increasing the direct public sector spending on key economic and social infrastructure, to at least 6 per cent of GDP by 2020;
- minimising bid-costs for infrastructure provision/financing to ensure the broadest possible range of engagement by potential investors (including simplified and streamlined processes for smaller investors in infrastructure);
- minimising the political risk associated with investment in infrastructure, in particular 'start-stop' decision-making, and changing the processes, rules or other key elements of a project once underway;

- expanding the use of privatisation or other mechanisms for the transfer of existing and prospective infrastructure assets to the private sector, including 'capital recycling' (using revenue from the sale of existing infrastructure assets to fund the development of new infrastructure); and,

- developing and marketing, as appropriate, public infrastructure bonds as tradeable financial instruments on terms and conditions which appeal to a broad spectrum of investors.

8 Funding - Private Sector

8.1 Master Builders' supports a broader and deeper role for the private sector in infrastructure supply in Australia. However, this should not simply substitute for inadequate public sector infrastructure supply especially in non-economic (but still fundamentally worthwhile) and/or social infrastructure which is the proper role of the public sector.

8.2 The private sector can contribute to closing Australia's existing and prospective infrastructure deficits by, inter alia:

- more efficient provision of current infrastructure through, for example, the privatisation of existing infrastructure assets; and/or;

- supplying, whether in the form of construction, operation and maintenance, appropriate infrastructure, in particular of an economic nature, beyond that provided by the public sector alone (the 'additionality' test).

8.3 Master Builders notes calls for greater engagement by superannuation institutions in financing infrastructure assets, whether by:

- purchasing existing infrastructure assets (that is, privatisation; with revenues being used for 'capital recycling'); and/or,

- funding the creation of net new infrastructure assets ('additionality'), either directly or indirectly (through the purchase of special purpose tradeable financial instruments).

8.4 While Master Builders shares the wider business concern at the inadequacy of our national infrastructure base, we remain firmly of the view the:

- primary function of Australia's superannuation industry is to maximise retirement incomes for superannuation fund members;

- with investment strategies and practices of superannuation institutions directed solely toward delivering the optimal risk-return outcomes for fund members.

8.5 Against this background, Master Builders would oppose mandatory requirements for superannuation institutions to invest (or not invest) in any particular asset classes or products. Rather, Master Builders considers infrastructure to be one of a range of potentially suitable asset classes which a diversified superannuation fund could constructively consider for allocating some part of its investment profile.

8.6 Key elements of a robust reform agenda which are properly the function of the private sector include steps by:

- financial institutions and other investors to broaden and deepen their capacity to evaluate the absolute and the relative merits of infrastructure as an asset class, and specific infrastructure projects as investment vehicles within a diversified investment/lending portfolio;

- financial institutions and other investors to obtain better information on opportunities for investing in infrastructure, either on their own, through relevant industry or professional associations, and in conjunction with counter-parties in the infrastructure supply chain; and,

- the financial sector more broadly, including the investor community and infrastructure providers, to create tradeable financial instruments, such as private infrastructure bonds, which could be used to finance infrastructure projects in denominations which appeal to a broader range of investors (in particular, smaller investors).

9 Funding – Infrastructure Charges

9.1 Until the 1980s, the provision and funding of urban infrastructure was the primary responsibility of local (but also to varying degrees, State) Governments.

9.2 Since then, and reflecting growing fiscal constraints on Local and State Governments, this responsibility has increasingly been shifted on to the private sector, in particular the developers of 'greenfields' and/or 'brownfields' sites.

9.3 This burden has been reflected in what has become known as 'infrastructure' (also generally known as 'developer') charges.

9.4 That is, requirements and associated costs being imposed on property developers for the supply of mandated urban infrastructure, ranging across basic infrastructure (such as local roads, water mains), and major head-works (such as arterial roads and water pumping stations), but also extending to community-wide social infrastructure (such as parks, play/sports grounds and libraries).

9.5 Master Builders does not, as a general rule, cavil with the broader principle underlying appropriate application of 'infrastructure charging', that is efficient user pays, accompanied by greater accountability, transparency, and contestability.

9.6 However, the application of infrastructure charges by State and Local Governments in general across Australia has fallen well short of what would have been reasonably expected by the building and construction industry, and by home-buyers who ultimately bear the costs of such charges.

9.7 Research by Master Builders (Master Builders 2009) found developer charges in growth areas of Sydney could amount to as much as $66,000 - or around 30 per cent of the sale price - for a single vacant block of land zoned for residential development.

9.8 Key problems with the imposition of infrastructure charges range across:

- de facto taxation: where infrastructure charges are used by State and Local Governments as a back-door means of raising general revenue, rather than efficient user pays, then
    - such imposts are essentially a tax, and work to discourage development and housing supply (Henry, 2009).

- This adverse effect is likely to arise when the infrastructure charges do not reflect the true (avoidable) cost of infrastructure supply.

- ('Avoidable' infrastructure charges are those efficient user pays-based costs which would not be incurred if the development did not proceed.

- adverse effects on housing supply and affordability: where infrastructure charges are poorly designed or administered, or operate as community-wide de facto taxes, they can reduce housing supply, raise housing prices and exacerbate housing affordability problems.

9.9 As the Henry Tax Review (Henry, 2009: 428) concluded:

> *"… where infrastructure charges are poorly administered - particularly where they are complex, non-transparent or set too high - they can discourage investment in housing, which can lower the overall supply of housing and raises its price."*

- promote uncertainty: ad hoc and/or inconsistent infrastructure charging policies and/or practices can result in increased uncertainty for developers, which are inevitably reflected in higher-than-otherwise required rates of return on prospective property developments.

9.10 Such issues are particularly problematic for developers engaged in 'urban infill' projects, whom can be 'called upon' to fund/undertake upgrades of (loosely associated) infrastructure, such as local railway stations and pedestrian bridges.

9.11 They can be particularly problematic, even pernicious, when the infrastructure charges are imposed/increased on the developer after they have purchased the land and/or made other irreversible commitments to the development.

9.12 'Gold-plating': which arises when State and Local Governments mandate developer charges to fund more infrastructure and/or infrastructure to a higher standard than is efficient or required.

9.12.1 This situation can occur when State/Local Governments wish to 'cross-subsidise the future'.

9.12.2 'Gold plating' is particularly liable to occur during election years, with marginal (narrow-margin-to-lose) and/or populist State/Local Governments.

9.13 The 'free rider' problem: this situation occurs when the residents of existing suburbs, whose infrastructure costs were met from general revenue paid by past generations, are able to use, without contributing to the cost of providing, new infrastructure.

9.13.1 For example, the residents of 'the old part of the suburb' are able to enjoy the use of new play/sports grounds, parks or libraries, funded by infrastructure charges borne by recent arrivals to 'the new part of the suburb'.

9.13.2 Such arrangements, essentially, provide residents of established suburbs near to infill developments with windfall gains.

9.14 Master Builders has identified a number of solutions to inefficient infrastructure charges[4] , ranging across:

- disallowing developer charges which undermine housing affordability objectives - all Local Governments looking to impose developer charges be required to receive relevant State Government authorisation, based on the assessment the proposed charges do not undermine housing affordability;

- greater transparency in infrastructure charging - providing comprehensive and detailed information on, inter alia, developer charges imposed by each and every State and Local Government across a range of property developments;

- mandatory public disclosure of developer charges - to promote consistency, transparency and accountability, and reduce the risk of corruption, in the area; and,

- abolition of rate caps and review exemptions - which impede the ability of Local Governments to raise general revenue which can be used to fund infrastructure, adding pressure on them to resort to developer charges.

[4] For a more expansive discussion, see Master Builders (2009), a copy of which can be found at Attachment B.

10 Conclusion

10.1 Master Builders in this submission has examined, and proposed reforms, which will help to address Australia's infrastructure shortfall.

10.2 A number of these reforms will require bold policy action; political will.

10.3 They include, but are not limited to:

- more efficient investment in critical infrastructure, most notably transport infrastructures;
- effective workplace relations laws and policies, in particular restoration of a robust Australian Building and Construction Commission (ABCC);
- increased government (public sector) funding of priority economic and social infrastructure, to at least 6 per cent of GDP;
- minimising bid-costs for infrastructure provision/financing to ensure the broadest possible range of engagement by potential investors (including simplified and streamlined processes for smaller investors in infrastructure);
- minimising the political risk associated with investment in infrastructure, in particular 'start-stop' decision-making, and changing the processes, rules or other key elements of a project once underway;
- expanding the use of privatisation or other mechanisms for the transfer of existing and prospective infrastructure assets to the private sector, including 'capital recycling' (using revenue from the sale of existing infrastructure assets to fund the development of new infrastructure); and,
- developing and marketing, as appropriate, public infrastructure bonds as tradeable financial instruments on terms and conditions which appeal to a broad spectrum of investors.
- removing the barriers to greater private sector investment in infrastructure, by a broad spectrum of potential investors; and,

- ending inefficient 'infrastructure/developer' charges, which inflate housing prices and retard property development.

11 Bibliography

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