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Value Capture in Australia
Ideologies, Methods, and Analysis

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Table of Contents

Executive Summary iv
Introduction 1
Section 1 Analytical Framework 3
- Sources of Infrastructure Funding 3
- Forms of Value Capture 4
- Sources of Confusion 5
- The Framework 8
- Criteria for Evaluation 9

Section 2: Betterment Levies 12
- Theory of Betterment 12
- Interaction of Planning and Value 16
- Valuation Practice and the Betterment Levy 18
- Rejection of a Betterment Levy 21
- Evaluation Criteria for Betterment 24

Section 3 Development Contributions for Infrastructure 28
- Theory of Contributions 28
- Intergenerational Equity 30
- Linkage between Betterment and Infrastructure 31
- Nexus and Exchange Value 35
- Australian Contribution Levies for Growth Areas 40
  - Victoria 41
  - Queensland 44
  - New South Wales 46
  - Other States 49
- Analysis of Indirect Benefits 50
- The Method of Differential Valuation 53
- Proportionate Sharing 59
- Point of Incidence 60
- The Effect of the Triggering Event 63
- Negotiated Contribution Levies 64
- Capacity to Pay 68

Timing of Recovery 69
Government Cooperation for Unlocking Value 70
Evaluation Criteria for Development Contributions 75
Section 4 Land Taxation 80
Theory of Land Taxation 80
Use of Property Taxes as a form of value capture 81
Evaluation of Property Taxes for Infrastructure 84
Section 5 Recommendations for Australian Value Capture 86
Recommendations as to Betterment Levies 86
Recommendation for Infrastructure Development Contributions 86
Recommendations as to Property Tax 88
Section 6 Operational Choices for Value Capture 89
Revised Development Contribution Framework 89
Property Tax for Growth Infrastructure 90
References 91

Executive Summary

Value capture methods must be analysed according to Australian history, governmental arrangements, ideology, and sensibilities and not by methods employed overseas.

Betterment is not an appropriate means of value capture in Australia as it does not accord with contemporary views of planning ideology and, as well, is administratively difficult.

The infrastructure contribution levies in use in Australia are defective in ignoring a nexus between the benefit and contribution, and interlacing inappropriate betterment charges. They need to be revised.

The use of Voluntary Planning Agreements in New South Wales is inconsistent with all proper bases for value capture and has no place as a value capture method.

Land tax is the best value capture method for infrastructure and can be combined with a revised infrastructure contribution scheme if there is legislative amendment.

Introduction

The place of value capture to fund infrastructure is very confused in Australia. In fact, it has been confused for over 100 years. The confusion arises because of a multiplicity of value capture methods used around the world all of which have different underlying bases, mechanisms, and practical effects, and accordingly are poorly understood by Australian governments and the community.

In the period of 2012 - 2013, there was a plethora of reports in Australia that focused on considering value capture by resort to successful overseas practices in the United States, the United Kingdom, Japan, and Hong Kong. The Infrastructure Finance Working Group provided advice to Infrastructure Australia in 2012 to use value capture as one alternative for funding based entirely on U.S. examples. In that same year, the South Australian Office of the Economic Development Board in *Major Infrastructure Funding Alternatives* promoted consideration of the funding methods used overseas. The manner to carry out value capture in a local context was only speculative at this time as indicated by the Business Council of Australia's *Securing Investment in Australia's Future: Infrastructure Funding and Financing* of 2013. The High Speed Rail Advisory Group in 2013 *On Track: Implementing High Speed Rail in Australia,* doubted if value capture was at all an effective form of funding for new rail.

The efficacy of the various value capture systems is not understood by merely copying overseas experiences but rather it is dependent upon the ideological, ethical, and legal issues that form the basis of Australian society. These issues are not capable of being pushed aside by saying value capture is a good idea because the state now finds itself in an era of rapidly increasing costs for infrastructure that it must fund or on the basis that the system has worked well in other places. In the last three years especially, as methods have appeared to be successful in other countries, value capture has become just that in Australia: a good idea used around the world to fund infrastructure that now is perceived as applicable everywhere. In 2015, the World Bank elevated the idea by actively promoting that value capture was to be regarded as a critical method for funding infrastructure in developing countries

(Suzuki, Murakami, Hong & Tamayose 2015). The moment that value capture is labelled such a good idea, that it seems right and that it has been proven in overseas case studies, and this is such a moment, then its scope and use is treated as boundless. Layers of local and state levies are then imposed for any situation in which funds are needed. A landowner has little to say in terms of infrastructure choices yet their property becomes a bank for funding every rail, road, or social imperative, such as affordable housing.

The purpose of this paper is to break through the confusion by investigating the historical, ideological, economic, legal, and planning concepts behind value capture used to fund infrastructure and growth in Australia in order to suggest a proper basis for the use of different mechanisms and their implementation. For the choice of methods to be grounded, they each must fit within Australian legal norms, ethical considerations, and traditions.

The thesis of the paper is that each method of value capture must be extracted, examined, and then understood in its own context in Australia. It is not enough to lump the methods together.

Section 1 Analytical Framework

Sources of Infrastructure Funding

There are four broad categories of funding infrastructure in Australia:

Federal Funding: investments and grants from the federal government into infrastructure through formal Infrastructure Investment Programmes and Grant Programmes, carried out through the *National Partnership Agreement on Land Transport Infrastructure Projects* of 2014 between the Commonwealth and the States. This traditional funding is derived from taxes, such as capital gains tax, GST, and other forms of revenue, all of which form a pool of funds, some of which can be allocated for infrastructure.

State and Local Funding: local government property taxes for local services, as well as state land tax and stamp duty creating a funding pool, some of which can be allocated for infrastructure.

Direct Funding: includes public-private partnerships, user charges of tolls or fares. These are funds available specifically for establishing and maintaining infrastructure.

Levies: a one-off charge paid by a landowner on the basis of receiving an uplift in value or receiving the benefit of infrastructure.

Forms of Value Capture

The essence of all value capture forms is that they are focused on capturing *value creation* where the land is increased in value by the actions of government. They are not concerned with *value realisation* where the owner makes a profit by productivity, such as building flats and selling land at a profit. This value realisation will be captured by other forms of tax, such as capital gains tax or stamp duty, but they are not methods of value capture for the express purpose of funding infrastructure. Value capture for funding infrastructure focuses on externally induced value increases.

Value capture in Australia has three forms that vary depending on the reason for the increase in value that is to be captured:

Betterment: The increase in value due to planning decisions is captured. This occurs multiple times; as examples:

For Greenfield sites:

1. At the time of earmarking the land in a plan or policy for future growth;
2. At the time there is a detailed plan for an area such as a precinct plan;
3. At the time land is rezoned from rural to a residential or other use;
4. At the time there is subdivision approval;
5. At the time there is development consent;

For Brownfield sites:

1. At the time land is rezoned for a higher use such as residential;
2. At the time there is subdivision approval;
3. At the time there is development consent;

For Urban Areas:

1. At the time land is zoned for a higher use such as high rise;
2. At the time the Floor Space Ratio permits higher buildings;
3. At the time of development consent.

Infrastructure Contribution: The increase in value that is the basis for the contribution is due either to the present or future provision of infrastructure from which a benefit is or will be derived by the landowner making a contribution. As an example, if a landowner is close to a future, planned train station, the developer will derive a future benefit and is therefore subject to a contribution.

Land Tax: The cause of the increase in value is not relevant but rather the increase that is captured is reflected in the non-specific accretion of value of the land over time: property tax captures a percentage of that yearly increase in value.

Sources of Confusion

There are at least six fundamental sources of confusion in understanding value capture forms:

Causal Interlacing: The future promise of infrastructure may be cause for an increase in value due to the planning system, interlinking betterment with a contribution derived from infrastructure. As an example, when an area is earmarked as a growth area in a strategic plan, there is an implication that infrastructure will be provided. The Sydney Metropolitan Strategy of 2005 that established Growth Areas, also indicated the infrastructure necessary. In this case, the

increase in value is due to the designation of land as the proximate cause but the provision of infrastructure is also a cause. In the same way, a zoning change will cause value increase, which is then captured by a rise in the property tax.

Temporal Causes: Betterment and the actual benefit of infrastructure may arise only in an uncertain future, yet are captured in the present. The promise of future infrastructure may cause an increase in value, as could a promise of resulting future zoning changes. This occurs because the system of strategic planning in use in Australia operates on the assumption that increased population must be dispersed into new areas as well as existing ones. As a result, areas are marked in strategic plans for future growth before they are ready to be developed and this alone will cause an increase in land values even though no development is yet permitted.

Overseas Comparisons: As most governments world-wide seek developer contributions for infrastructure, various methods have been attempted. These methods are based on cultural nuances related to property rights and the relationship of the citizenry to government. It is confusing to talk about successes or failures elsewhere when they may or may not be applicable to Australian sensibilities and institutions.

Methodological Causes: The value generated by land placed in a growth area can be captured by betterment, an infrastructure contribution, and property tax. The infrastructure contribution can be applied as a general rate without regard to the specific infrastructure involved or can distinguish between uses, suggesting a betterment charge. A land tax can be administered by policy to take into account the highest and

best use of the land, making it a form of betterment. Each method can be bent to the particular purpose, most often without explicit recognition of what method is being used. This has led to viewing value capture as an amalgam of methods and has not encouraged examination of each method and its appropriateness.

Orientation: From the perspective of the pressing need for funding of infrastructure, some of the deficiencies of value capture are glossed over and the methods are expanded and not analysed, causing uncertainty and confusion. From the perspective of a landowner or developer, the details of the derivation of the levy, the point of incidence, and the timing of payments are critical. The shift from one point of view to another – from government to developer - changes the efficacy of an exaction, its operation, and its success.

Seeking all value: With techniques available for value capture for all three forms, a planning authority may blend them all to maximise funding. There is a tendency to capture every bit of value as a source of revenue. For example, the report *Transit and Urban Renewal Value Creation for the City of Sydney* (LUTI 2016), suggests that the value created by the benefit of increased accessibility to infrastructure plus that from changing zoning by that increased infrastructure and then adding an increase in development density applied together will result in willingness to pay for the infrastructure, zoning, and development intensification. This idea combines two types of betterment (zoning and density increases) as well as infrastructure contributions (benefit of accessibility). It is hard to answer the question of whether this is efficacious when the parts may have different orientations and mechanisms.

The Framework

The forms outlined are those primarily in current use in Australia. Each method has a different ideology, a different history, and different ethical considerations. These factors are the only means to distinguish one from another. In practice, because of the various sources of confusion, the mixture of methods does not discern what is being captured and why. In the rush to exploit land value increase, governments are not able to explain why they have chosen a particular method and just return to the idea that funds are needed so value must be captured.

The appropriate framework is to evaluate the three methods to understand which of them appropriately forms the bases for the value capture methods used in Australia. There is a strong case to be made that referencing methods used overseas is not helpful in the Australian analysis as they have to do with particular planning cultures, such as broad based betterment charges in Bogota, Columbia, or a system of transferable development rights in New York.

As each value capture method has a different ideology and purpose, it is important to know which method is being advanced in the complexity of legislation and the consequences. This is because each has different nuances, administrations, situational appropriateness, and most critically, efficacy.

This framework suggests five steps:

1. Evaluation of betterment charges;
2. Evaluation of Infrastructure contributions;
3. Evaluation of property tax;
4. Recommendations.

Criteria for Evaluation

The value capture methods that are analysed, to be understood and evaluated, must be held up to explore their ideological bases, their fairness, and their efficiency in operation.

Ideological Bases:

The concept of capturing the value of land has a long history but each form has different ideological underpinnings and operates according to a different view of property rights. The differences in the forms can be accounted for in terms of alternative ideologies.

It may appear in the rush to find ways to capture value that to examine the general ideological and philosophical underpinnings of the forms is of little use as it is merely theoretical with no practical purpose. However, it is an essential exercise to understand what are the legal and ethical issues that are the appropriate bases that are most suitable for value capture; the necessity to take this route is explained well in an analysis of value capture by the U.S. think tank *Lincoln Institute of Land Policy*:

> "The mechanics of capture have proved troublesome…. At least one approach to solving the conundrum is to recognize that attitudes toward land value capture are intimately linked to the ways in which the concept of "property in land" itself is understood. This in turn requires us to consider how property has been constructed in law and the philosophical and constitutional underpinnings of such constructions" (Booth 2012, p. 74).

Test of Fairness:

The concept of fairness relies upon underlying societal values and has a particular place in Australian history and culture. The degree to which a landowner can be charged to pay for government services is always under scrutiny, as witnessed by the capping of rates in New South Wales and Victoria: "…it must be acknowledged that rate capping is not just a technical exercise but an understandable political

response to apparently ‘excessive’ rates increases especially in times of relative economic constraint and low inflation” (McKinley 2015, p. 8).

As a fundamental principle, fairness requires that each individual receives a proportional benefit from the contribution they pay towards infrastructure. The examination of what is fair is particularly important with the current shift away from traditional funding with the entire burden on government, to an emphasis on obtaining funding from landowners.

Equity in relation to value capture has not been an important, explicit subject of discussion in Australia. Its presence is there as a backdrop to value capture, as can be witnessed by the recent Queensland “Fair Value Infrastructure Charges Schedule 2015” and the “fair go” rating system of Victoria. The concept of fairness includes “distributive justice,” which suggests there is a fundamental need for an equitable distribution of public goods and public burdens, as well as “social justice,” described as a fairness element that is necessary for the proper functioning of society (Kuehn 2000).

In the United States, the issue of fairness has arisen specifically in the case of value capture for road and rail. However, it has not been resolved: “…equity is an ongoing and evolving concern that will need to be addressed over time through many and diverse decisions that will often involve trade-offs between benefits and costs” (National Research Council 2011, p. 15). The most that can be accomplished is to measure the value capture method in two respects:

1. Benefit: is the landowner, the subject of the exaction, receiving a benefit from the amount paid;

2. Proportionality: is the amount paid proportionate, having regard to others, to the cost of the infrastructure.

Efficiency:

"Adaptive efficiency" is the name given to the economic concept of whether a value capture method is conducive to economic growth. Accordingly, any value capture method that impedes the market because of its inefficiency in operation or effect, will be less efficient than one that does not impede the market.

The three criteria overlap in all instances. Efficiency of procedures may become more important than fairness or the positive ideological motivation of a method may not be carried forward because of difficulties in respect of efficiency. Yet the alignment of these three is perhaps the most that can be asked for in respect of any interference with property rights through value capture.

Section 2: Betterment Levies

Betterment is the term used to describe a value capture method where the increase in value that is captured is due to the *operation of the planning regime*. It is not used as a means of value capture in many countries. However, it has been in planning laws in Australia since 1928 and it still underlies a rationale for value capture.

Theory of Betterment

The philosophical underpinning of betterment is that the value of land, a focus of value capture, arises from the ability to exploit opportunities on land. This basic concept is reflected in the 19th century reliance on Richardo's theory of "economic rent" (Murray 1977) that parcels of land have greater value (rent) because of increased productivity on the part of the landowner: land with a crop is more valuable than vacant land. The capacity to exploit land to increase its value arises from the nature of land ownership; it is not a separate or subsidiary right but rather it is intertwined in the fundamental western idea of property.

The legal reflection of this theory is that the capacity to increase the value of land is recognised by the courts and therefore can be said to be a component of a proprietary interest in land. It is proven as a proprietary interest and a fundamental right in Australia by the requirement that there be payment of compensation on "just terms" under the Constitution (section 51(xxxi) reflecting any increase in value when land is acquired compulsorily. In Queensland and Western Australia, the loss of value to a landowner by a planning restriction that reduces the capacity to exploit land is also subject to compensation.

The consequence of land value as intrinsic to property ownership is that a productive owner can increase the value by hard work. In modern, developed cities, productivity on land occurs by incurring developments costs in building or improving land by a higher producing use but in fact these factors may ultimately be less important to the increase in value that arises from a wide range of area amenity factors (Albouy 2015). Even in rural areas, productive value is more dependent on

water, climate, and soil than merely hard work (Harris & Hanson 1950). Nevertheless, this idea that an owner can increase value by productivity is at the heart of value capture theory because if there is no increase in the economic rent caused by some productivity in any form, then there will be no levy or tax to be paid.

This concept of economic rent is the foundation of the ideas of John Stuart Mill who recognised that there is a difference when land is increased in value by the actions of the state and not merely by productivity. In 1874, he drew attention to the "Future Unearned Increment Increase of the Rent of the Land ... or a great part of that increase, which is continually taking place, without any effort or outlay by the proprietors, merely through the growth of population and wealth . . ." (Mill 1874, V.5, p. 225). He proposed that this unearned increment does not belong to the owner, based on the theory of rent and that it was not earned by productivity, and must be returned to the state. Mill's democratic liberalism was at odds with individualism and private property and was followed by the socialist sentiments of Henry George and the Fabians. The ideas of Mill and Henry George resonated in the struggle of the worker with the elite structure of England. Winston Churchill in a 1909 address to Parliament stated:

> "Roads are made, streets are made, services are improved, electric light turns night into day, water is brought from reservoirs a hundred miles off in the mountains — and all the while the landlord sits still. Every one of those improvements is effected by the labour and cost of other people and the taxpayers. To not one of those improvements does the land monopolist, as a land monopolist, contribute, and yet by every one of them the value of his land is enhanced. He renders no service to the community, he contributes nothing to the general welfare, he contributes nothing to the process from which his own enrichment is derived."

This philosophy and political sentiment became reality in the UK *Housing and Town Planning Act 1909* that provided for a "betterment tax," initially to be 50 per cent of the increase that could be traced to government regulatory changes. According to the "Practical Guide" accompanying the Act, the increase was to be measured by "a comparison of the full value of the property immediately prior to and irrespective of

the scheme with the full value of the property immediately after the making of the scheme' (p. 50).

It is important to embed the theory of betterment in its cultural and philosophical context. Henry George, in proposing a betterment tax on unearned wealth, was proposing that there is an *injustice* “which condemn the producer of wealth to poverty and pamper the non-producer in luxury….” (George 1879). His underlying idea, taken to its logical conclusion, was that the entire city belongs to the community and not just individuals having property interests. This “right to the city” idea, made explicit by Henri Lefebvre (1991), is that the only true justice in a city is if all the value belongs to every resident. In a modern exposition of this view in light of value capture systems, it has been suggested that it is just and equitable that all gains in land value be distributed to the public, especially if they are the result of government action (Fainstein 2012). By this theory, systems where the government owns all the land and provides leases are the most efficient as shown in Amsterdam or in a modified version through profit sharing as occurred in the redevelopment of 42nd Street in New York (ibid, p. 35).

The UK Act provided for capturing a 50 per cent increase in the value arising from a planning scheme when it changed the use of land to one that was more lucrative for the owner; what would be referred to in Australia as a rezoning. In the same way, the Act provided for a situation where value was lost, proposing a 100 per cent payment of compensation to the owner when their land loses value by a planning scheme, as when productive land is earmarked for public open space.

The ideology behind a betterment levy was never made clear through the legislative history of the English experiment with value capture: the ideas of Mill and Henry George were never expressed as applicable. The underlying theme that unearned increments belong to the state was, however, the unarticulated basis of its origin and casual acceptance, as for instance in the New South Wales *Local Government (Town and Country Planning) Amendment Act 1945* where these concepts were introduced.

As a matter of administration, the degree to which land was bettered or suffered was too complex to calculate and eventually the levy was discontinued. However, the idea of betterment remained attractive because it was congruent with the ideology of the land law of England. This is because the English land tenure system is predicated on a single holding of property being split into diverse interests, such as mortgages, leases, and easements: the existence of another interest such as that created by planning was conceptually possible and could be justified. For this reason, at least, the dormant betterment levy was reintroduced and increased to 75 per cent in 1932. However, unrest as to its administration and purpose continued and the schema was revisited by the "Expert Committee on Compensation and Betterment" (the Uthwatt Report) in 1942.

The touchstone for the Uthwatt Report was that every decision in a planning scheme creates a 100 per cent shift in value so that some will benefit and others will suffer. The idea in Uthwatt is that the shift occurs because demand for each type of use is finite so that if it is removed in one place, it will appear in another. Therefore, a system of compensation and betterment had to be balanced. The practical consequence was that payment by the government for compensation or collecting betterment from a landowner for development consent depended upon making decisions on where development should be allowed, thus leading to the modern UK system of development control to balance the relative interests.

A United States commentary on the Uthwatt Report made the observation that "When compared with the traditional rights of private property, these proposals are, to say the least, drastic" (Spengler 1942, p. 20). They represent, according to the author, a "hostile tariff" on development and proceed on an incorrect analysis of land value:

> "The fundamental defect of the proposal is that it fails to take any account of the economic nature of land value. The accretion of land value which may take place in any particular site during the next five years is no different in nature from the value which it has already acquired. It is entirely due to the whole economic environment including the public services available, the density of population and the general economic activity of the community" (ibid, p. 23).

This must be understood from the United States perspective of the sanctity of property rights, fundamental to the American enterprise. From this point of view, the concept that the value of land can be taken by the government was anathema. Yet it prevailed in different guises in the UK through various devices as for instance a Planning Obligation: an undertaking to pay various contributions if development consent was granted. Eventually, various reports and committees saw this as a tax on development (Booth 2012, p. 84) and explicit betterment charges were no longer exacted.

The initial planning legislation that brought betterment into the early Australian planning legislation was modelled on the English system, as filtered and interpreted through the first Australasian legislation of New Zealand in 1926 that included a direct provision for betterment (Section 30). In many ways, the betterment provisions were an accident arising from following the English and New Zealand structures as there was no debate or consideration about betterment provisions in the first planning legislation that followed, which was the Western Australian *Town Planning and Development Act of 1928*, that contained a betterment provision. The concept was included in this and other planning legislation without any mention of the efficacy of compensation and betterment, the difficulty of balancing the two, or the underlying economic rent rationale.

Interaction of Planning and Value

The concept of betterment developed alongside the view that planning decisions were a single enunciation of the best planning outcome for the land. If a decision was made to allow a four storey building on a vacant lot, it was a planning decision that increased the value of land. If land is zoned for say, a residential use where before it was only for a light industrial use, the value of the land appears to be increased by the planning system.

In some systems, as in the UK, there is no zoning but rather each planning decision is subject to a separate decision, a system referred to as “development control.” In

other systems, as in the U.S., zoning creates development opportunities as of right. In Australia, there is both zoning and development control. Some uses may be permitted as of right but most are subject to an application for development consent in which the zoning is a relevant consideration. In Australia, changing zoning will only provide an inchoate value and not a manifested value if development consent is also required.

When value is manifested, there is only value creation and not value realisation. The development still needs to be built and sold or used. This means that a landowner, if there is a betterment levy, is asked to pay at the time of creation and not realisation. This is the case in all betterment levies as the state deems the creation of value as the basis for the increase in economic rent and the point at which there are unearned increments.

Betterment assumes that the state or local government is making a rational decision to increase the value of land. It does not take into account that the choice of boundaries between one zone and another may be arbitrary or that the decisions may not merely be a simple allocation of land uses but are the effects of political influence, community protests, attempts at increasing the rate base, or even corruption.

The assumption of the betterment levy is that it is the planning system that, even if influenced by internal factors, is delivering a benefit, which is an increase in land value. This, however, ignores the modern conceptualisation of how land use decisions are made. The general economic situation, say of a recession or high unemployment, may affect the choices made by developers and planning authorities. If a city becomes attractive to business over many years, this may result in an increased population and the need for new housing on the urban fringe. It is not then the planning regime that is creating the benefit of increased value but the general economic and political situation manifested in planning decisions. It is also the case that development opportunities arise outside the planning system, such as restrictive entertainment venue laws in Kings Cross, Sydney, changing the character of an area to permit more valuable uses. A decision by a developer to build a shopping centre may benefit owners of land nearby but value is enhanced by the

decision of tenants who bring a certain quality to the area. A national imperative, such as mitigating greenhouse gases by cutting emissions, may result in areas being freed up for healthy living. The placement of a nuclear facility can lead to a rapid decrease in land values in nearby areas. In the case of growth centres in Australia, the decisions are made based on population projections, of which 26.8% of the population are immigrants; the immigration policies of the country bear significant responsibility for the creation of growth areas to accommodate housing.

The planning system is the servant of these larger agendas and it is not possible to say that it is the actual cause of the gain but rather it is the vehicle for implementation. It is only the proximate cause of the gain as the regulatory system is the point of contact between the community and the factors that lead to the planning changes. These planning changes are in turn based on various theories of the proper spatial allocation of land uses that affect choices for land use but are constantly in flux. For instance, central place theory suggests that retail shopping should be concentrated in a single area that services a wide catchment, resulting in decisions for large box shopping centres that is the norm in Australia. This central place theory is a "gravity" model that calls for concentration of uses related to consumer behaviour and has now fallen out of favour to be replaced by more localised, main street shopping ideals. In this gravity model of aggregation of uses, the variables of land use choice are even more imprecise and can depend on geographical barriers, such as topography or land suitability, environmental variables, such as contamination or habitats, social variables, such as movements of population or income levels, existing urban variables, such as the transportation networks; public interest variables, such as health or safety; and demographic variables, such as existing patterns of settlement.

Valuation Practice and the Betterment Levy

Land value arises from a combination of these planning, social, and economic variables, aggregated and arranged in a land use pattern, which by its nature, is imprecise and approximate (El-Barmelgy, et. al. 2014). The consequence is that it is difficult to argue that payment should be made by an owner for planning gain as the

causes of the unearned increment are external in terms of general government policy, are random, and depend on shifting theory as well as unconscious ideologies. An example of such an ideology would be a desire for a city to promote itself through massive high rise buildings even though it does not accord with any sound planning reason, as is proposed for South Perth.

The unanswered question in levying planning gain is whether it should be based on the use that has been given development consent or on the highest and best use to which it might be put; the unearned increment may lie more in the development potential than what was approved. The highest and best use is very much the manner in which land is valued in Australia when it is acquired compulsorily. A descriptive example is the history of the acquisition of land owned by Walker Corporation at Ballast Point in Sydney by the Sydney Harbour Foreshore Authority. In the Land and Environment Court, [2009] NSWLEC 219, the market value of the land was said to include the potential for accommodation of aged persons at one figure, or a lesser figure on its current zoning for industrial uses. The method used was to indicate what a willing buyer would pay a willing seller at its highest and best use. It was necessary in establishing value to traverse through the entire planning history of the site in order to determine the potential use and whether the large range of matters for development consent for residential accommodation for aged persons would have been forthcoming. This was a highly speculative result that even the judge called a "best guess."

The formula used in the early New South Wales betterment provisions in the *Local Development Contribution Act 1970* was derived from the need for infrastructure under the Sydney Region Outline Plan and the valuation was from a specific date (1 August 1969) until it was rezoned. If a person purchased land after it was rezoned, any increase thereafter was not levied. The Sydney Region Outline Plan indicated where growth would take place in the region. This method was based on a recommendation of the *Report of the Royal Commission of Inquiry into Rating, Valuation and Local Government Finance in N.S.W.* of 1967. It recommended this limited method of timing the period of value uplift because of the failure of the general method in the 1945 New South Wales *Local Government (Town and Country Planning) Amendment Act* to just value any increase caused by a scheme.

This limited form of betterment levy: establishing the difference in value of land of land before and after zoning, is the only possible use of a betterment levy and it is clear why this form was selected. If the period is not precise and related closely to the uplift event, in the complicated system of modern planning, the policies, trends, precedents, state interventions, and a myriad of factors would require analysis before it can be said what indeed is the unearned increment as years go by and land is eventually developed.

The valuation of land in the 1970 Act was based on unimproved capital value, carried out by the Valuer-General in the same way as land rates are calculated. This ignored the highest and best use of the land and the improvements made and just used the standard valuation as the means of assessing value for betterment purposes. There are indeed other methods of valuation, such as the accounting concept of the net present value of the enterprise applied to the use of land or the economic concept of discounted cash flow. Net present value or book value is the sum of all historical outlays, less the sum of the total depreciation booked against the outlays. Discounted cash flow is a projection of the cash flow reasonably expected less the cash expenditure, which reflects inflation and risk and yields a rate of return calculated on alternative investment opportunities. These methods of valuation are complex and would have to be applied if the levy was seen as efficacious. Accordingly, using unimproved capital value, made the administration of the levy possible.

The British betterment levy in 1968 was on the value of land with development consent, less the value without consent. As there was no zoning or area designation as with the Sydney Region Outline Plan, the levy was concentrated on value from the development consent. It should be pointed out that there was reluctance to reintroduce the levy because in 1965 a Capital Gains Tax was introduced meaning a person was taxed twice on profits. However, as a method that valued the before and after value of development consent, it was very much “subject to doubt,” particularly because of the difficulty in ascertaining the value before development consent (Harriss 1972, p. 570). This value required a judgement on what would have been the use to which land could be put in any event: its highest and best use that a

willing buyer would factor in as a market value. There was also a realisation that the increase was not necessarily attributable to the development consent, but as already suggested, it may have to do with general economic conditions making such a levy less than logical.

The ability to train valuers in the method of assessing development potential of a particular zoning in a system of development control is limited as it is complex and not easily understood. The number of factors that should be considered in assessing the development potential of land is vast and includes issues, to name a few, such as accessibility of social services, shopping opportunities, and the quality of the existing built form. It can be done with the help of planners but is not often teased out by reference to all variables. To use a valuation technique based on unimproved capital value also does not account for all of those factors that may be relevant in land value increase.

The valuation on unimproved capital value versus development potential is a comparison of "current value" with "fair market value." Current value is measuring the value of land according to its current use not its potential. Fair market value is measuring the amount a willing buyer would pay a willing seller taking into account all possible uses to which the land could be put. The third method is the "economic value" that is the fair market value and the subjective value, and is especially important in the market price arranged for residences. The "project value" may be important in particular cases as it is the value due of the infrastructure that is added to the other forms of value. This lack of assessment accuracy is what profoundly complicates the use of a betterment levy.

Rejection of a Betterment Levy

A betterment levy, based on Mill's idea that there is an unearned benefit that must be recovered, is no longer in favour both because it has no clear, modern theoretical underpinning and also because of administrative difficulties in calculating a planning uplift. As a funding source, it is unreliable as it is not possible for an infrastructure agency to predict what would be the amount and timing of recovery as this depends

on valuation at the time of development consent for uses that are not predictable. In 2009, a World Bank report on value capture methods summarised the current use of betterment levies:

> "The 'tax' rates imposed by betterment levies—30 to 60 percent of the gain in parcel value attributed to public investment—are so high that both public opinion and the courts have rejected this form of infrastructure finance unless there can be greater certainty about the underlying land-value gains. For this reason, betterment levies have fallen out of favor as a significant source of revenue" (Peterson 2009, p. 6).

The pure betterment idea, built on the philosophical argument of returning unearned increments to society, aside from the difficulty of administration, was perhaps weakened, at least in the United Kingdom, by neoliberal values of personal wealth creation. The concentration on the benefits of wealth creation and the corresponding requirement of less regulation became the rubric of planning. This is not explicit but can be seen in the outright dismissal of betterment by the neoliberal champion Margaret Thatcher in 1967: the betterment levy, she asserted, was "a particular group of financial provisions which received more criticism for complexity than any I have ever known, even exceeding the criticism of Corporation Tax and Capital Gains Tax" (Hansard HC [746/359-69]).

The reasons why betterment failed is given as complexity of administration and valuation but It also had other effects that caused it to be unpopular. In the New South Wales *Land Development Contribution Management Act of 1970*, the betterment levy was proposed of 30 per cent of the price of sold land or the increase in the value of land arising from development consent. The levy was bound to fail on the basis that land prices increased as those who were liable passed along the very high levy in the sale price and, as this was not always acceptable in that market, owners held back on developing or selling land hoping the Act would be repealed (Archer 1976). Its short life indicates that an underlying reason for its failure was that it was seen as an imposition on private property rights in the nature of a tax.

A method for betterment levies in Australia has been suggested based on the capitalised value of infrastructure and also valuing the external benefits from development consent (Fensham & Gleeson 2003). The capitalised value is fully determined by three factors: the benefits that individuals have already paid for by rates or user charges such as parks or local roads, the social infrastructure component of schools and hospitals that already are paid for by taxes and excises, and amenity factors that have arisen by access to services and markets. At that point, additional value arises by development rights through approvals. This is the "surplus" that arises over and above taxation investments made for infrastructure. The argument is made that reducing this to another form of tax on all residents is to neglect that a betterment levy on development consent is more directly related to the provision of infrastructure generated by what is proposed. The suggestion is then that there be a betterment levy applied to the realised increment associated with the capitalised value of social infrastructure plus the access to external benefits granted by development consent. The idea says nothing about how that value would be calculated at the point of incidence. However, it is a realistic appraisal that something more than unimproved capital value must be as the base of a betterment levy as the owner has already paid for some benefits in other forms of taxes and charges and there is a differential between landowners as to the benefits received.

The Henry Tax Review (2010, p. 424) rejected a betterment levy for several reasons: the benefit to the developer is difficult to determine, value may increase before rezoning in anticipation making the true valuation difficult, negotiations on the amount of the levy will slow down development, it increases uncertainty as to the development process, governments may be encouraged to upzone land to recover a levy, and developers may slow down the productive use of land. Of all these reasons, the difficulty of tracking value is the most compelling.

The key to a betterment levy as compared to any other form of value capture is that it is dependent *solely upon a planning system* changing or allowing a change in planning opportunities that affect the economic rent. Its origins therefore reflect a simple view that planning itself changes the value of land. In all cases, it is clear that value is created as well by the economic situation, demographic patterns, shopping centre policies, and the myriad of other factors that relate to the existing and

proposed amenities of the area. These cannot be easily valued and therefore, properly applied, the search for value will become administratively impossible. A levy on unimproved capital value ignores these factors and is as inaccurate as a levy that attempts to unpick all of the relevant, complex variables that account for value in individual land holdings.

Evaluation Criteria for Betterment

Ideology: The ideology of capturing an unearned increment created by the planning system is not consistent with the manner in which value is created by modern planning theory. This theory looks at the city in relational terms, concerned with place making, concentration on social capital in communities, resident participation, and interactive local networks. It is no longer purely a Euclidian process of drawing areas on a map and turning some on for growth.

Benefits are considered to arise by the creation of amenity values to do with place and community and this is a proximate cause of value increase culminating in development. As well, the idea that planning itself is creating value is no longer sound as the economic condition, immigration, interest rates, and environmental concerns have a role to play, making planning decisions the trigger for value creation but not the cause. The value attributed to a planning decision therefore cannot be accurately isolated in many cases solely because of a change in zoning or development consent. The example found in the Lockout Laws in Kings Cross that have resulted in an increase in value to adjoining areas without any change in planning is an easily accessible answer. In fact, other, seemingly extraneous factors have been found to increase value significantly, such as gay and lesbian residents (Christafore & Leguizamon 2012), cultural activities and artists, school quality, historic preservation districts, and other factors that produce a subjective experience of an area. These factors cannot be set aside in order to determine what is the pure, residual value arising from planning.

In the UK, where betterment levies were conceived, they were based on balancing compensation and betterment in a system of development control; there was no

system of zoning so that land was bettered only to the extent that it reached a higher value by the consent. The UK system of balancing compensation and betterment developed from a theoretical idea that there is a 100 per cent shift in value when development consent was granted. This is inapplicable to Australia as the increase in value is also caused by the zoning and, as well, there is no matching scheme for compensation linked to betterment, nor is there ever going to be as this defeats the modern purpose of value capture as a form of revenue.

In Australia, the regimes require a two-stage sequence: there is an uplift by the zoning itself or switching on the area for development, and then development consent. The unearned increment is there when the area is rezoned but is not levied at that point but on some future triggering event. In the case of development consent as the common trigger, consent itself increases value (as that consent enures to the benefit of a subsequent purchaser) and accordingly the value is doubled in effect – once by zoning and again by consent.

The difficulty of having the value as two components is that If the development does not take place for some time awaiting detailed planning, the value continues to rise because of choices not only made by the planning authority for that area but priorities and resource allocation for other areas. As well, there are decisions made by other developers that may accelerate growth in an area, create a particular standard of development, or may attract inhabitants over other areas as the locality matures. When it comes time to pay the amount, it may be that the developer is paying one increment for creeping value and another for the distinct advantage at a fixed time for obtaining consent. This means that the betterment levy in all cases is based on value extraneous to the planning system and not just that arising from a saleable development consent. The creeping value is unable to be quantified as to what it has brought and how the value is then calculated before development consent and after.

If the area is not rezoned or left out of a growth area, it suffers a distinct loss of value. This is ignored as merely a regulatory restriction that is an acceptable intrusion on property rights. However, it is a distinct consequence of planning just as is betterment. To have a system that ideologically is based on the shifting of value

by planning and then ignore one side of the equation, reduces it to a device with no theoretical underpinning.

Fairness: The sentiment that it is fair to capture value caused by the planning system is one that is present in any egalitarian oriented society, such as Australia. The fact that developers could make gigantic profits by being in the right place when an area is rezoned for intense development is antithetical to those struggling financially or who have adjoining land that is not up-zoned. Using fairness as a touchstone for a betterment levy is useful as it seeks to differentiate unequal value caused by extraneous forces beyond productivity. However, the fairness in this respect is negated by the percentage charged of the increase in value. This percentage on nothing tangible and on a consequence of regulatory decisions that are outside the control of the landowners makes the levy seem in fact unfair. The Productivity Commission reports that the betterment levy of 0.2 per cent of unimproved capital value of users of the Sydney Harbour Bridge and the 1963 levy for the Melbourne Underground Rail Loop were put under political pressure and removed (Productivity Commission 2014, p. 165), no doubt for this underlying sense of unfairness.

Confining betterment to growth areas allows landowners in other areas to reap the benefit of planning decisions with no consequence, except of course capital gains tax or increased rates. The spatial disequilibrium means that the levy is not market-neutral as prices will undeniably be differently affected in competing areas because of the levy. As well, there is temporal disequilibrium because some owners who must pay the levy will pay less depending on their obtaining consent earlier than others.

There is no method of knowing what is the appropriate percentage because the calculation is not based on supplying infrastructure or services where the total amount can be proportionally spread over the land that is capable of being developed. For a betterment levy that has no particular financial goal, the percentage becomes a political issue and often fails for that reason.

Efficiency: The valuation of land as a base for betterment is only clear when it is levied on unimproved capital value. In this instance, the valuation without the zoning

or development consent can be calculated and the land value thereafter can again be understood. This, however, is only capturing just the land increase and not the highest and best use created by the planning system. If development consent is given for a use that is less than the highest and best use, the landowner and the state are only receiving a portion of the potential value. When the highest and best use is taken into account, the exercise is very complicated due to the myriad of factors that might indicate a particular use, such as draft schemes, policies, and government policies. Betterment levies will fail because of the difficulty of administration and therefore are inefficient.

Section 3 Development Contributions for Infrastructure

Theory of Contributions

The responsibility of a developer to contribute to infrastructure arises because there is a need to internalise an external consequence to the community (increased traffic, noise, impact on services) arising from the development such that it would be unfair for those externalities to be absorbed by the market. This is an economic concept that requires that the market corrects the externality by making it a cost to the developer in return for the benefit of permission to develop.

If costs were not internalised or made the responsibility of the developer, the consequence is that there would have to be a subsidy by the community for that development to proceed. The subsidy would take the form of a tax, the burden of which would be borne by the entire community, even though the cost came from the development.

The options are bifurcated: the developer contributes to the externality it creates or the externality is subsidised by a tax. The need for the former depends in turn on the economic concept that there will be a transfer or fleeing of capital to avoid a higher tax. The importance of preventing capital movements and encouraging market equilibrium is at the heart of the internalisation, as markets generate and sustain urban economic potential. Markets seek “allocative” or Pareto optimality so that they are said to be efficient when a person can be well off with no one worse off, meaning internalisation is necessary. The consequence is that internalisation can be applied to individual developers because they are creating an externality but otherwise, the burden must be uniform across the community so that it does not result in the movement of capital.

The theory of market efficiency does not permit passing on a burden to be borne by the community so as to benefit individuals. This would result in development distortion as there would be scattered spatial effects on land prices and population

migration (Brueckner 1986). As a consequence, the group of individuals that must bear the burden are those who are called upon to internalise an externality that *they create.*

The need for a direct link between the externality and the particular development was indeed the basis for all exactions in the United States. The direct link between a project and its externalities changed primarily in the 1980s to broader impact fees for infrastructure requirements in an area not directly caused by a development. The change, it is suggested, came from many sources: environmentalism and social movements demanding more from developers, cutbacks in federal aid, concerns about the infrastructure backlog, and perceptions that the levies will be absorbed into the market (Altshuler, Gomez-Ibanez & Howard 1993, pp. 123-124). When it is related to a specific area even wider than a local government area, the historic theory of externality internalisation is able to be justified.

The theory holds true in all situations when the infrastructure necessary is able to be identified. Even in the case of a wider area where the infrastructure that is needed or the infrastructure that arises from future potential development is derived, the nexus remains remote but justifiable. Where there is no mention of the infrastructure or the infrastructure is outside the area and the monies are put into a general fund with no relationship to an infrastructure plan, then there cannot be said to be a connection and the theory of externalities has no importance. In that case, the levy is based on land being designated as within an area that will receive some benefit in the future, the nature of which is not known. This is a statement that the land is being benefited by the planning system, which will require infrastructure in the future and is more in the nature of a betterment theory of an unearned increment. In these situations, when the externalities theory is lost, the purpose of the levy is “at best blurred” (ibid, p. 134).

The Productivity Commission (2014) expressed the values that are inherent in infrastructure contributions:

> "In principle, developer contributions should only be made to the extent that infrastructure is attributable to the properties being developed. This is straightforward for infrastructure that is clearly related to a developed property, such as that linking a property to a local network. It is less straightforward for networked infrastructure shared with other developments, such as water mains. Ideally, the incremental cost attributable to each property would be reflected in developer charges (pp. 171-173)."

The concept of a link between charge and infrastructure is considered to be so important that the costs ideally should be apportioned for each landowner. The reason is that the basis for expanding externalities still remains "user pays." This is tied into the framework of Rawl's (1971) theory of justice that there be "horizontal equity" or fairness among users. The notion of "justice" in Rawl's ubiquitous ideas are that it equals equity and includes equal opportunity and treatment of individuals. This principle is so well established that it does not matter if horizontal equity conflicts with economic efficiency (Jannson 2001).

Intergenerational Equity

One of the principles of "sustainability" is that of intergenerational equity so that present actions do not damage future generations. In environmental terms, intergenerational equity is part of "sustainability" or, as it is called in New South Wales, "ecologically sustainable development." If there is a development contribution scheme, the question arises as to the effect of a levy on the original owners and future owners of land.

When land is first increased in value by being earmarked in a growth area or zoned for a higher use, the landowner is receiving an uplift in value. When that land is sold *before* it is developed, the purchaser is paying not only the uplift ('U') but also a potential premium, discounted for risk, that will arise from development consent ('DC'), and the added amount that new infrastructure will bring ('NI'), less the cost of the infrastructure contribution fee ("IC"); the price is therefore: P = U + DC + NI – IC.

In this formula, NI is independent of the actual cost of the infrastructure or its replacement cycle; it is a gross estimated benefit. NI, however, is difficult to value as

it is dependent on the nature of the infrastructure, as a new sporting ground will differ in effect than a road. The value of the infrastructure, however estimated, is depressed by the contribution that has to be made as well as by land value taxation that is a continuing stream into the future as value continues to rise. If the rates are capped, then there may be a discounting based on deteriorating infrastructure.

The value of the infrastructure to a purchaser is the discounted net benefit stream. At the time of development consent, it is merely capitalised and then added to the value for further on-sale. The reality then is that the landowner who has purchased property in an area marked for growth has already paid uplift and also for the infrastructure in part so that the original owner receives a windfall. The consequence is that infrastructure contributions benefit existing owners who receive that windfall as does each subsequent owner when property is sold prior to the full development of the area and implementation of all infrastructure. The development contribution benefits the previous generation and burdens future generations as the unbuilt infrastructure costs will continue to crystallise and be passed on in future sale prices.

Linkage between Betterment and Infrastructure

The formula for intergenerational equity is an illustration that there is always a link between uplift by planning change and infrastructure. When there is no linkage because there is no estimation of future infrastructure, a planning change may still result eventually in increased infrastructure, such as an area zoned for high density living eventually requiring a transit connection. However, the connection between infrastructure and a levy in this case is only an assumption and is missing several details. For instance, the infrastructure may be proposed in the future as a wish list of what is thought necessary and the priorities may not be made specific. This is particularly the case in Australia where there is a lack of refined coordination between infrastructure agencies and planning.

To understand the relevant linkage between betterment and exactions, it is necessary to return again to theory. The now classic but highly theoretical studies of the effect on land value by the provision of infrastructure explain clearly that when

there is *local* expenditure on public infrastructure, the value of land increases by the amount of the expenditure. The studies also investigate the situation where the residents differ in location in respect of the infrastructure and in all cases, the differential values still reflect the infrastructure, except perhaps on the border of a city (Arnott & Stiglitz 1979; Arnott 1979; Henderson 1985). These analyses were based on proving the "Henry George Theorem." The Theorem is not referring to the idea of capturing unearned increments of which Henry George was a champion, but rather that government spending on public goods, such as infrastructure, will increase land value more than that amount.

These theories were derived in relation to a single area and require the existence of a perfectly symmetrical situation, where each group will be similar in terms of the benefits received. A critical theory that can be applied to a wider area is the "Tiebolt Model" that concludes that individuals are more likely to be drawn to one community over another if it has better infrastructure services but less tax: the provision of services creates added value but that is decreased if taxes are higher. The Tiebolt Model refers to a differential "head tax," which is a lump-sum tax on some individuals and not others that approximates a modern infrastructure levy. When applied to a region, the inefficiencies of a head tax are that regions with smaller resources will be less populated than those with greater capital. The Henry George Theorem is therefore only correct if sites are identical and, when they are not, individuals "face an incentive to reside in the resource-rich regions to share in the benefits of those rents, so that local taxation of land (broadly defined) loses its efficiency properties" as it results in population movement and capital differentiation. (Mieszkowski & Zodrow 1989, p. 1139).

As the theory points to the negative effect of infrastructure provision across a wide region, it suggests a wide area property tax. Such a tax is then a price at which residents purchase infrastructure even though it becomes a distortionary tax on capital, as it has a greater effect on residents when land has more value. However, when land tax is applied as well as an infrastructure levy, it will, according to theory, drive capital from an area as the tax differential will distort the allocation choice for capital. This theory suggests that the two choices: a land tax and a head tax both have distortionary effects. The difference between them is significant. A land or

property tax as a general tax on land according to a derived rate, does not depend on the precise outcome by a formula of the amount of money needed for infrastructure divided by the amount of land but rather can be a figure totally ascertained by a general budget determination. On the other hand, a levy that is related specifically to infrastructure must find its validity in the nature and cost of the infrastructure and the effect on the value of properties that bear the levy.

The levy derived from supplying infrastructure cannot depend for its efficacy on a general betterment argument that the whole area will improve and land values will increase but rather on a *nexus* between what infrastructure is needed and what benefit will be received. An explanation of the Community Infrastructure Levy that commenced in 2010 in the UK explains its justification in terms of infrastructure and benefits:

> "Almost all development has some impact on the need for infrastructure, services and amenities - or benefits from it - so it is only fair that such development pays a share of the cost. It is also right that those who benefit financially when planning permission is given should share some of that gain with the community which granted it to help fund the infrastructure that is needed to make development acceptable and sustainable" (DCLG 2011, para 7).

The New South Wales Special Infrastructure Levy was created with a similar idea pursuant to Section 94EE of the *Environmental Planning and Assessment Act 1979.* The Section allows the Minister to create a levy under the circumstance where "the Minister is, as far as reasonably practical, to make contributions reasonable having regard to the cost of the provision of infrastructure in relation to the development …." (Section 94EE(2)(a)). When introduced in 2006, the then Minister Sartor stated: "

> "developers may undertake intensive, simultaneous development. This creates a need for councils and the State to concentrate funds to ensure that infrastructure and amenities are available to complement such development" (Hansard 10/4/06, Second Reading Speech).

If there is a property tax, it not derived from the benefit that will be conveyed but solely by the need for infrastructure generally and a nexus is unnecessary. The choice of one or the other has different consequences brought about by the nexus criteria. Historically, the move away from betterment to an infrastructure levy was a variation on the Mill idea of a tax on an unearned increment to instead creating an exchange value proposition consisting of two forms. The first form is that the developer is paying a share of the cost because it requires infrastructure to develop, which the government is supplying. Secondly, a levy is imposed because the developer is benefiting directly from the infrastructure. Both of these propositions imply that there is an actual nexus between the infrastructure and the gain. This is a critical shift that has occurred in the theory and practice of value capture.

The reasons for justifying a levy are subtle and can lead to ideological confusion. The propositions in the statements in the UK and New South Wales introducing the levy, and there are others, suggest that when there is a benefit obtained from *planning permission*, there is a need to contribute to infrastructure that will service that development. It is putting it on the basis that the development is what creates the need for infrastructure but implies that there is a connection between planning gain and infrastructure and, if development goes ahead, this will lead to services. This may not be the case for practical reasons. In New South Wales, as an example, there is little direct coordination between transport decisions and land use planning. Unlike “area-oriented” planning in the Netherlands or “Infrastrucktur in der Landschaft” in Germany, there is fragmentation between planning decisions and roads and rail. Infrastructure provision is an externality to planning and more of a hope than a certainty as the agencies have long, committed agendas that often precede planning decisions. It is only when there is attention to that fragmentation that it can be said that there is coordination across different spatial scales and agendas. As present, there is a closed governance model that does not exploit synergies of infrastructure and land use, except perhaps informally. The consequence is that there may be only an indirect relationship between development consent and infrastructure. Research has shown that when there is integration, value then emerges in terms of certainty and developer choices (Holland 1998). Without certain integration, the value increase is speculative.

It is also inaccurate to assert that there is always a cause and effect relationship between development and infrastructure. Forward commitments for a rail link may ignore the vector of development and that vector may be more opportunistic than coordinated. This is especially the case when a planning authority must make a choice of where to place housing on the urban fringe. In the case of New South Wales, the growth centres chosen for increased housing are proceeding at a haphazard rate and the choices of which land to release may be a function of the timing of Precinct Plans that contain the finer details or expediencies to deliver a backlog of housing.

The pillars upon which value capture rests in Australia are no longer patent. The move away from betterment to value capture by infrastructure levy started as having the basis of a clear nexus, either real or hoped for, between the infrastructure supplied and the benefit to land. However, as the lack of coordination of infrastructure with planning has become more patent, the nexus is often forgotten or is now merely a platitude and levies, amounting to a land tax for ever-widening designated areas, have emerged as practice.

Nexus and Exchange Value

A direct and provable nexus between a contribution and infrastructure is a fundamental development in the law of Australia. This is echoed clearly in legal decisions in other places as well.

In the United States Supreme Court in *Nollan v. California Coastal Commission*, (483 U.S. 825 (1987)), a condition to supply an easement to allow the public to enter on private land for a view of the ocean was said to be invalid if the condition "fails to further the end advanced as the justification…" and the comment was made that building regulation was not a valid regulation of land if it was "an out-and-out plan of extortion" (ibid, p. 834). This doctrine emerged from the historic practice of requiring a special assessment on property to pay for improvements that provided a direct and special benefit to the property. On this reasoning, wider impact fees, where an amount was paid as an assessment of the future costs the development will have

were allowed. “Linkage fees” went even further and provided that the approval of central city developments (usually commercial or office space) had an impact on a developer's need for facilities or services.

Nollan was decided in the context of a different history of exactions than Australia. The *Standard City Planning Enabling Act* in the U.S. that contained the provisions for developer exactions based on a nexus came into use in the late 1920’s and was considered critical in the context of local government bond defaults in the depression of the 1930’s and the need for external funding of infrastructure. From that time on, in spite of the increased use of exactions, the fees have required a rational nexus with the infrastructure arising from the impact of the development.

The rational nexus test confirmed by *Nolan* had two parts. The first is that there must be a reasonable connection between community growth that new development generates and the need for additional facilities to serve that growth for the exaction to be valid. If that was the sole basis for the test, it would accommodate wide-area growth levies as found in New South Wales. However, the second test was that there must be a connection between the fees imposed from development and the benefits that development will enjoy. The burden fell on government to show, among other matters, that the infrastructure provided will benefit the contributing development. A classic analysis of these tests (Nicholas & Nolan 1988) indicated that the result is that the government need not show that a developer exclusively benefits but that it substantially benefits and this includes proof that the landowner will actually use the infrastructure and that the funds collected will be spent in a reasonable time.

Since *Nolan*, another decision of the U.S. Supreme Court, *Dolan v. City of Tigard* (1994, 114 S. Ct. 2309) emphasised the test of “proportionality:” a reasonable degree of proportionality between the fees charged and the cost of expanded infrastructure. This has to be precise and not merely a conjecture. This has led to reliance on “marginal cost pricing” where the need for the nexus means that those who are responsible for the development bear the cost of infrastructure that they necessitate.

There is a narrow approach in some cases that requires a stringent test of nexus and others where a wider, "rational relationship" is said to be more important. In an early contribution case (*Blue Jeans Equities West v. City and County of San Francisco*, 3 Cal. App. 4th 164, 4 Cal. Rptr. 2d 114 (1992)), it was found that that a levy under the San Francisco Transit Impact Development Fee could be applied even where the benefit was not clear. In this case, the landowner affected was not located near the transit system but it was found that the fee applied because it was in the general geographic area that would benefit.

The English standard for development exactions, which became the Australian standard, was set out in the House of Lords decision in *Newbury District Council v Secretary of State for the Environment* (1980) 1 All E.R. 73, quickly followed in New South Wales less than a year later in *St George Building Society v Manly Municipal Council* (1981) 3 APAD 370. The essence of the tests as relevant here is that a condition of development consent must "fairly and reasonably relate to the development for which permission is being given." The question of relationship or nexus has come up in many decisions and as it relates to value capture, the decision in *Cardwell Shire Council v King Ranch Australia Pty Ltd* [1984] HCA 39; 58 ALJR 386 is most important. An applicant for subdivision of 600 hectares into nineteen blocks was required to contribute an amount to upgrade a bridge and to extend a bitumen road some distance from the property. The lower court judge found that there was no nexus between the exactions and the subdivision. The High Court concluded:

> "It does appear that he considered that the conditions could be imposed only if they were necessary to provide access or drainage to the land or if they provided a benefit to the land which would be enjoyed exclusively by persons connected with the land. This is a test more stringent than the law allows…."

The two modifications arising from this decision are that it need not be shown that the contribution was necessary or provided an exclusive benefit, meaning that the nexus exists when the infrastructure itself was necessary and there was some benefit to the community. The benefit can be indirect but there still must be a nexus. The nexus must be demonstrated before the reasonableness of the exaction can be

considered: *Cavasinni Constructions Pty Ltd v Fairfield City Council* [2010] NSWLEC 65 [33].

In *LWP Property Group and City of Swan* [2012] WASAT 129, the effect of these decisions are expressed clearly:

> "A condition cannot arise solely from the existence of a public need which bears no relationship to the subdivision. The requirement that a condition reasonably relates to the subdivision does not, therefore, allow the Commission or the local authority to use the subdivision or development as a trigger for a future need that does not arise, in part, from the project. There is no justification for the use of conditions to promote the community infrastructure simply because the developer has come forward for approval ..." [72].

There is a no recognition that a state imposed developer levy in any form should somehow override a nexus requirement. In a 2005 decision in Queensland (*Hickey Lawyers (a firm) & Ors v. Gold Coast City Council* [2005] QPEC 22), it was stated:

> "There is no principle that I am aware of that requires the ratepayers or a council's general revenues to bear the costs of providing and maintaining infrastructure required to service new development. The general thrust of evidence and the unfolding of statute and case law considered in the appeal is to show steadily increasing sophistication in levying charges against developers, who will doubtless "pass them on". The trend has been that some difficulties identified over the years in this court and its predecessors have been surmounted in various ways. I think there is nothing untoward about this" [34].

This case concerned an infrastructure levy policy of the Gold Coast council that imposed a high charge for recreational facilities and transport. The *Integrated Planning Act* repeated the *Newbury* test that there must be a nexus. The policy used the methodology of identifying the ultimate population that will be in the city, the infrastructure that will be necessary to service the population, then dividing the city into sectors where there is a distinct level of transportation use, examining trip generation to determine the number of trip ends in each sector and charging the developers the cost attributable to their development.

The issue of how indirect the benefit can be cannot be explained by implying what has been allowed and what has been refused by the courts in particular instances. It appears that, at its highest, if the differentiating of areas for the purpose of establishing relative benefits occurs, this is a recognition that there is some nexus proposed between the exaction and the benefit. The benefit in the Queensland case found its legitimacy in the measurement of relative trips in each sector, an explicit statement that the cause of the development will be to generate more trips and, to the extent that those trips are measured, the developer must pay.

This sentiment that the developer must pay is especially the case in Australia because of the system of development control. The planning authority has a chance to meet the developer with contributions at the time that they seek consent to develop, which represents an expression of their desire to create value and a chance to evaluate externalities. In Australia, the rights that arise with property ownership only have the character of the granting of a inchoate privilege because of the need for development consent or subdivision approval. This idea that the actual right is only crystallised at the time of consent and subdivision has been part of Australian heritage from early legislation and decisions of the courts (*Ex parte Forssberg; Re Warringah Shire Council* (1927) 27 S.R. (NSW) 200). Accordingly, the levy can be directly related to the actual development.

In contrast, in the United States, development consent is not the primary means of land use control so there was no direct trigger for an exaction. The origins of exactions in the early 20th century in the United States were in fact focused on externalities on subdivision approval but then progressed to wider exactions resulting from the formation of large subdivisions or, as they were called, “official map acts” or benefit assessment districts that required approval of subdivision for a defined area. Exactions were only reluctantly accepted in these cases because property ownership is a right that carries with it the capacity for carrying out appropriate development without consent in zoned areas. Accordingly, there was a need for specific legislation to allow exactions as it was not congruent with these rights and a system without development consent and could not somehow be implied as a legitimate

exercise of local government powers (*Enchanting Homes, Inc. v. Rapanos*, 143 N.W.2d 618 (Mich. Ct. App. 1966).

This property rights versus privileges analysis, although not articulated in these terms, allowed a subtle shift in Australia between the strict need for a benefit that is direct and an acceptance of a benefit that is indirect arising as an externality. The fact that a developer merely receives an indirect benefit from that future infrastructure has been ignored historically in contributions schemes arising from the infrastructure arising from drawing a boundary around a particular area. The reason perhaps is that the plan boundaries are logically derived from an area having common characteristics where the uses proposed are interrelated. This is a logical extension of regional planning where the operational or functional relationship of the constituent areas creates a similitude of land interactions. This idea of planning and envisaging an authority for a wide area is a characteristic of Australian local government and planning history; for example, the City of Sydney was joined in 1948 with eight inner city municipalities by the *Local Government (Areas) Act.* If you have a defined area, the reasoning would then say that being present in that area is the basis of deriving a benefit from infrastructure; inclusion amounts to a benefit.

Australian Contribution Levies for Growth Areas

In Australia, the historical basis for contributions from landowners has always been a user pays system where the developer is contributing because of the use of existing infrastructure or the developer supplies infrastructure as an externality resulting from the proposed development. No other rationale, aside from failed betterment schemes, has ever been put forward. The systems of contribution levies, extending the nexus to larger, growth areas, which is their current form, are of recent origin and have developed between 2004-2016. Initially, they were oriented to be an extension of the user pays idea that a developer was going to be the direct user of the infrastructure and therefore was providing a contribution as exchange value for the infrastructure. A brief summary indicates a country-wide change of approach and a loosening of the nexus requirement.

Victoria

In Victoria, there was the Environmental Contribution Levy in 2004 for water businesses based on a user pays model. A local development contribution levy system was in place since 1995, where there was a requirement of a direct nexus between the exaction and the infrastructure supply. Part 3AB of the *Planning and Environment Act 1987* adds a general "user pays" sentiment to a system that provides that a planning scheme can include infrastructure contribution schemes. The essence of the contribution scheme is to fund: "the provision of works, services and facilities in relation to the development of land in the area to which the plan applies" (Section 46GB(1)(a).

The weakness of a levy's application for larger, growth areas, was made clear in the Victorian Civil and Administrative Tribunal in 2002 in *Dennis Projects PL v Wyndham CC (Amendment)* [2002] VCAT 1117. Although this case is not heralded as the reason for change, it appears to directly address the need for a wider ambit for levies for the first time. In this case, a developer wished to develop 148 hectares near Werribee. The Council imposed a condition that the developer contribute to regional drainage, not just local or consequent drainage. It was argued that, based on the *Newbury* case, there was no nexus between the condition and the development. The argument was put by the council that the land was part of the region and therefore enjoyed the benefit of regional drainage to which it should contribute. The Tribunal stated: "The sort of infrastructure projects which can conveniently be made the subject of a development contributions plan in a planning scheme are of the much smaller and more finite kind, similar in scale to the street construction schemes which are frequently the subject of Tribunal hearings [70]." The Tribunal stated that it was constrained by the 1995 Act for local development levies that required a distinct nexus but, most importantly, the Tribunal stated that it believed that the argument that the land was part of the region and should be levied in this way was in fact correct.

The growth centres infrastructure development levy was introduced in 2010 to the *Planning and Environment Act 1987* and Hansard debates recount great opposition to the 2010 Bill as a tax imposed in advance of any proper planning for the growth

areas (Hansard 2 February 2010). The Growth Areas Infrastructure Contribution (GAIC) provisions went further than any previous exaction and provided that the Minister should calculate the amount of the levy for different types of land that must be paid in the growth areas by a triggering event. The events are the sale of land, where the amount is paid by the purchaser, the subdivision of land, the receipt of a building permit, or an acquisition of a property interest held by an investment vehicle. The GAIC provides that the levy should be on all residential, business, and industrial land, and all land zoned in a form of growth area. There is *no mention* in 2010 that there must be any nexus at all between the amount that is set for the levy and the provision of infrastructure. The only connection perhaps is that the money raised goes into a fund to be used for infrastructure.

In 2012, an assessment of the system of infrastructure contributions was published as the *New Victorian Local Development Contributions System – a Preferred Way Forward* and led to a "Setting the Framework" document. It proposed a fixed standard levy for all areas, including growth areas: "A Standard Levy is proposed as the default in each development setting, but with the opportunity to apply a tailored Development Levy Scheme (in Growth Areas and Large Scale Strategic Development Areas) if strategically justified" (Report 1, p. 2). In 2013, a second report recognised that exactions under the Act had been too high and that there should be a pull-back on expectations as to the extent that levies can fund infrastructure. An Act was introduced in 2015 *(Planning and Environment Amendment (Infrastructure Contributions) Act 2015* that applies a standard rate for local infrastructure depending on the use of land, and a supplementary levy to be used when justified for additional infrastructure not covered by the standard levy. The Act retains the requirement that a *local* infrastructure contribution plan "relate the need for the plan preparation costs, works, services or facilities to be funded through the plan to the proposed development of land in the area." (Section 46GE (e)). These provisions are specifically excluded for Growth Areas.

The contrast between the local infrastructure contribution and the GAIC makes the lack of a nexus requirement clear in the case of Growth Areas. The contribution is not expressed as related to specific supply of infrastructure and the nexus is therefore only vague as there is a connection between the rate imposed and the

collection of funds used for infrastructure. This is a system that is not based on any explicit assumption that a developer is getting the present or future benefit of infrastructure. The fact that it is not applied until the triggering events can be said to imply that the developer will take advantage of the infrastructure provided and therefore must contribute; in terms of nexus, that is as far as it can be taken.

In the case of Growth Centres, the payment is by a purchaser of land meaning they buy the land with possible increased value due to the *future* infrastructure. Since the infrastructure connection is not related to the development and is not present necessarily at the time of sale, it may also be said to have changed into a betterment levy as it is the mere inclusion in a Growth Area that brings on the levy. A new purchaser is therefore obtaining land with the increased value due not to infrastructure but an uncertain potential for infrastructure meaning the real increase is from the designation as a Growth Area. The same is true for an organisation acquiring a speculative interest in land suggesting they are to be levied because they have bought into a Growth Area.

Without a nexus or an expressed connection, the GAIC is based on land being earmarked as within a Growth Area and therefore mixes betterment into an infrastructure contribution levy. Perhaps in the case of subdivision it can be said that there may be a closer link as the future infrastructure will be to the benefit of the owners in selling the land, as the purchaser will rely on infrastructure such as roads to service the density created by new lots. At most, there is a supposed benefit approach that assumes that the landowner will pay because the infrastructure will, as the Second Reading speech put it, “meet their needs.” On the other hand, there is a grab for speculator funds because of that triggering event, meaning that they are seen as taking advantage of an unearned increment.

This confusion is not explained in the parliamentary debates, the cases in Victoria, the published arguments about contribution levies, or the various reports that preceded the 2010 legislation.

Queensland

The Queensland Growth Management Summit of 2010 suggested that there be a Queensland Infrastructure Plan to integrate the regional plan (South East Queensland Regional Plan and Program and Far North Regional Plan) with the Roads Implementation Plan. This was consistent with the concept that Queensland growth and infrastructure be highly planned having regard to Transit Oriented Design. The government response: *Shaping Tomorrow's Queensland,* recommended the establishment of an Infrastructure Charges Taskforce. The *Taskforce* of 2011 proceeded on an assumption that coloured the shape of the charges. It stated in its Final Report:

> "The issue of who should pay for the funding gap then arises, with the public discourse generally focussing (sic) on whether it should be developers or the government. In many respects, this is misguided. Infrastructure charges are generally passed on to home buyers and individuals as ratepayers ultimately pay for the government contribution. In the long run therefore, the issue is not the apportionment of costs between developers and government, but rather the apportionment of costs between existing and new home owners" (p. 19).

Arrangements for charges commenced in 2011 by the *Sustainable Planning (Housing Affordability and Infrastructure Charges Reform) Amendment Act 2011.* This was a period characterised by intense activity to do with regional growth and regional infrastructure plans, such as the South East Queensland Infrastructure Plan. This was consistent with the need for priority development areas and viewing infrastructure charges in a wider sense.

In 2013, a discussion paper: *Infrastructure Planning and Charging Framework Review*, produced by the Queensland Government, suggested that it was proceeding on a "user pays" system and therefore there should be an "essential infrastructure list" on which the charge can be proportionally levied. The discussion paper led to a Priority Development Infrastructure Co-Investment Program in which the State indicated its share of investment and the *Sustainable Planning (Infrastructure Charges) … Act 2014* that set up the local government co-investment

program. None of these documents established the need for different forms of charges and were clear attempts to require “fair value” nexus charges related to the cost of infrastructure.

The *Infrastructure Funding Framework* was created under the *Economic Development Act 2012.* The Funding Framework is clear that one of its objectives is to “encourage development” and to make sure that new development in priority development areas (PDA) “fairly contributes towards the cost of providing infrastructure required to service the PDAs.” In relation to priority areas, the contribution includes an infrastructure charge for different uses, such as commercial and industrial, with a varying rate for residential and, as well, a “value uplift” charge. This uplift charge can be offset, as for instance in the case of commercial or retail development, where if economically sustainable development goals are met.

There is a clear mix of a development charge related to infrastructure and an uplift or betterment charge. The Act itself continues to provide only for a nexus as the levy in a PDA can be made if in the Minister’s opinion (Section 115(1)(b):

(i) The land, or the owner or occupier of land, has or will specially benefit from, or has or will have special access to, the service, facility or activity; or

(ii) The owner or occupier of land, or the use made or to be made of the land, has, or will, specially contribute to the need for the service, facility or activity;

In making the charge, the Minister must identify the land and the plan for the supply of the infrastructure. The Queensland system assumes that there is connection between the infrastructure and new development so that the infrastructure permits development and the development needs the infrastructure. The mixture created by the Minister of betterment and infrastructure connection is not made explicit but at most is derived from the broad wording of the Act.

For PDAs, the value is calculated when land is reconfigured (subdivided), and where there is approval for a material change of use. When a new lot is created in certain

areas, for example, Caloundra South, there is also a “special infrastructure levy” that is payable for 30 years.

The manner in which betterment and infrastructure contributions became combined in Queensland is because of a concentration on the absolute imperative of funding infrastructure and establishing a careful system for proportionate charging. There seems to have been no attention paid to the relationship of the betterment charge being used as an adjunct to the infrastructure charge. There is no document that suggests that the two are being combined. The *State Planning Regulatory Provision (adopted charges) 2013* that preceded the Framework did not contain any betterment provisions.

New South Wales

The New South Wales *Special Infrastructure Contribution* (SIC) follows on from Section 94 of the *Environmental Planning and Assessment Act 1979* introduced in 1979, although not used until 1989. Section 94 provides that local governments could create a contribution scheme for local infrastructure and require payment as a condition of development consent. The efficacy of the Section 94 levy is based on the contribution area being local in nature and therefore the possibility of the infrastructure benefiting the developer is clear. The exchange value is a local benefit for which there is a nexus.

In New South Wales, the expansion of development contributions (SIC) to wider areas in the same form as Section 94 can be traced to the Simpson Inquiry of 1989 that approved of the usefulness and efficacy of Section 94 (Simpson 1989). A review of the history of Section 94 indicates that it survived validity claims in the courts and the suggestion of Simpson was that the greater the nexus between the charge and development, the less likely would there be a further challenge (McNeill & Dollery 1999, p. 4).

The expansion of Section 94 in its present form occurred because of the Sydney Metropolitan Strategy. The Strategy was the first attempt to provide a strategic plan for Sydney along traditional lines of evidence-based population growth, projections

for housing, and the provision of infrastructure to accommodate growth. As the Strategy covered an entire region, choices had to be made where to distribute growth. As a result, Priority Growth Areas were designated with the intention of filling in those areas with more detailed plans. Fundamental to this gigantic undertaking was the need to supply infrastructure, as for instance a rail station at Leppington.

The work on the Metro Strategy reached a tentative stage of completion in 2005 and in 2006 Sections 94ED-94EM were introduced to provide for an extension of Section 94 to the Growth Areas. The Sections provide that they apply to the provision of essentially any form of infrastructure, such as affordable housing, transport, or "other infrastructure." The linkage occurs by requiring the Minister "as far as is reasonably practical to make the contribution reasonable having regard to the cost of the provision of infrastructure in relation to the development or class of development." The levy is a percentage of the proposed cost of carrying out development or any class of development. This is applicable for a special contribution area as determined by the Minister and the recovered money is held by the Department of Planning. An important requirement is that the determination of the Minister as to the levy contains the reasons for the level and nature of the development contribution. The Act sets up a Special Contribution Areas Infrastructure Fund under Section 94EJ. That Fund is administered by the Secretary of the Department in consultation with the Secretary of the Treasury to be paid out to public authorities for the provision of infrastructure.

As an example, in 2011, the Minister made the current Special Infrastructure Contribution Determination for the Western Sydney Growth Area. The Growth Area for which the Contribution applies are set out in a map in the Act depicting a vast area of land. The contribution is to be made for development on residential and industrial land not including a single dwelling or dual occupancy dwelling in the Growth Areas. The contribution is made patent as a condition of development consent. The projected infrastructure requirements were set out in carefully iterated detail in a Practice Note in 2010 and includes roads, rail, education, health, and open space. The amount payable is calculated by the formula: $\$C_p = NDA \times \$C_r$ where $\$C_p$ is the amount of levy that equals the net developable area (NDA) of proposed

development multiplied by a fixed development contribution rate ($C). Those rates that are set out in the determination are, for example, $205,258 per hectare of net developable area. In a 2008 Practice Note, the basis of the amounts was a calculation of the cost of works already provided as well as “the estimated attributable cost” of works yet to be provided.

The Metropolitan Strategy has earmarked land for growth and a calculation has been made as to the amount of infrastructure necessary. The underlying purpose is for a developer to pay for infrastructure that will be necessary as the land is developed. It is not a betterment tax on the basis of an up-zoning or a general land tax. It is interesting to note a comment in an explanatory brochure *Special Infrastructure Contribution: Western Sydney Growth Areas – Special Contribution Area* of the Planning Department in 2015 expressed the purpose as:

> “When land is rezoned to allow for more intense uses, there is an associated increase in land value. This increase is partly because rezoning means land can be used for higher uses, such as residential development, and also because the land will be supported by better roads, transport and community facilities and services.
>
> The provision of infrastructure to newly rezoned land is essential. The Government therefore decided that part of the cost of the infrastructure will be met by Developers who benefit from the uplift in the value of the land caused by the provision of infrastructure.”

This is an inaccurate statement, recalling betterment theory, of the otherwise clear basis of the NSW infrastructure levies, given its history and intent, as an exchange value of the developer paying for a benefit. It does highlight how easily the two concepts can be intertwined.

In local government contributions to infrastructure, there is a legislative requirement of a relationship or nexus between what is to be provided and development. However, there is no contractual commitment on the part of the authority to provide particular infrastructure in a fixed time line. Section 94 (3), for instance, states that a condition of development consent can be made for a levy where infrastructure has already been provided and when the development will benefit if the works will “if

carried out" be benefited. This indicates that the nexus may be vague but is still an identified basis for the levy. In the case of a larger area, the nexus is not as clear. The Marsden Park Priority Growth Area in southwest Sydney is 1,800 hectares and plans are for 10,300 homes. There is no question that infrastructure needs to be supplied, including the upgrade to Richmond Road, but what if the developer was further west near Stony Creek Road? In what way is that developer benefited? The answer could be that the fact that the land has been up-zoned, allowing the developer a chance for development is the real reason. However, that returns to the argument of a betterment tax. What is missing in large area contribution levies in large growth areas is some tangible exchange value – a benefit in relation to specific infrastructure, not merely a benefit arising from zoning.

Other States

In Western Australia, there historically were Guided Development Schemes that arose out of an interpretation of the First Schedule of the *Town Planning and Development Act 1928*. A system of infrastructure levies was created by State Planning Policy 3.6 *Development Contributions for Infrastructure* that does not apply to wide areas of land but rather is focused on discrete, defined local areas. The Policy provides: "The key principle is that the 'beneficiary' pays." This is explained in the Policy: "Consistent with this principle, developers will only fund the infrastructure and facilities which are reasonable and necessary for the development and to the extent that the infrastructure and facilities are necessary to service the development."

A contribution scheme was introduced for designated Growth Areas in South Australia under the *Planning, Development and Infrastructure Act 2016.* The reasons for the levy are a restatement of the fundamental nexus requirement (Section 163(2):

> "(c) the basic infrastructure is reasonably necessary for the purposes of development that is proposed or to be undertaken within the designated growth area (including on account of rezoning that has occurred, or is expected to occur, in relation to the whole or a significant part of the development that is to occur within the designated growth area);

> (d) the basic infrastructure will support, service or promote significant development that is proposed or to be undertaken within the designated growth area;"

It is observable that in all cases, except Victoria, there is a proposed connection between an infrastructure levy and development, suggesting that there is an exchange value for the charge. In all these instances, there is an attempt to settle on the amount of infrastructure that is reasonably necessary and to make sure, as expressed clearly in South Australia, that the infrastructure will support new development. These are referred to as "impact fees" or "development fees" and require the developer of land to internalise a portion of the infrastructure attributable to the infrastructure. In Victoria, there is a lack of a direct nexus but rather a form of tax, with the ability to pay capitalised by the land use proposed in a particular area.

Analysis of Indirect Benefits

The contribution schemes in use in Australia approach benefit in several different ways, sometimes overlapping, and more often implied rather than expressed. These benefits fall into two groups: those that imply that the infrastructure is necessary because of the development, and those that imply that the future infrastructure will supply a new benefit to the developer beyond that of existing infrastructure supply. In both cases, the necessity of supply and the benefit of supply will reach an outer limit where there can be no observable connection between the infrastructure and the development. When there is no benefit, an exaction is in the nature of a tax and not an impact levy.

All methods of value capture proceed on the basis that "Who Benefits Pays" system. A World Bank analysis in 2016 casts the net of benefit widely: general benefits received by society and therefore to be paid for by public authorities as representatives of the public; direct benefits received by users of the facility such as transport that can be charged to them as user fees or tolls; and indirect benefits: "Which are received by people that are nonusers of the system but still perceive benefits from the improvements in accessibility, mobility and increases in business

opportunities associated with the development of transport projects" (Ardila-Gomez & Ortegon-Sanchez 2016, p. 16).

The issue of nexus brings up the evaluative criterion of fairness. The World Bank analysis proceeds on the basis that all of the instruments for value capture must respond to various criteria of efficacy. One of these examines the effects of differential benefits, where an infrastructure decision creates a "winner" who obtains direct benefit from a contribution and a "loser" who pays but is too remote to receive an observable benefit. The notion of "equity," associated with fairness has two aspects: horizontal equity and vertical equity. The former refers to those who are essentially in the same economic situation having to pay the same levy and vertical equity refers to the proposition that those who have a greater capacity to pay or *receive greater benefits* should pay more (ibid, p. 20).

The need for equity and fairness by providing a charge against those who benefit of a greater amount and not against those who do not benefit at all relate back to the importance of value as an aspect of property rights. Although betterment is not used successfully as a value capture method, its ideology that there is an unearned increment still informs the ethical question of equity and fairness. It creates a natural differential between those who receive the greatest benefit and can therefore afford to pay more and those who receive little and therefore can pay less. Theoretically, the two are separate and benefit is related to nexus with greater access and not ability to pay.

The conferral of benefits can be defined as widely as any tangible or intangible advantages that settle on land by the provision of infrastructure. Capturing an increase in value because the area has been up-zoned is not a development levy but rather a betterment tax. Instead, conferral of benefits is a statement that a landowner will use the infrastructure or that the development proposed will require that infrastructure.

Presence in a catchment subject to a levy is not a guarantee that there will be a necessity or benefit. This is a critical issue in evaluating exactions. The choice of boundaries for a growth area, for instance, is not based on any planning theory but

rather upon an estimate of an area that can function as a whole. A landowner may fall on one side or the other of a boundary with no particular clarity as to the reason for the choice made. In order for it to be said that there is a necessity or benefit, the statement must be made that all members of the area will be advantaged by infrastructure. It could be argued that if an area receives infrastructure, it will then have an increase in value but this again is not helpful as it is a statement in respect of betterment; it creates a circular argument that the land is increased in value by inclusion in the growth area that will be receiving infrastructure and therefore must pay. However, the underlying principle of exactions is that there by some benefit arising for the developer not based on increased value. That benefit must be a statement that there will be an improvement *by the infrastructure* not by inclusion in the growth area.

If the infrastructure is actually required because of the development, then there is no issue of benefit and the obligation is clear. A development that will contribute intense housing will need road upgrades. This neatly fits with the *Newbury* case: the exaction reasonably relates to the development in the sense that the development will result in the need for infrastructure. The benefit can be either be direct or indirect but there is a relationship. When there is no relationship, it cannot be so justified. The World Bank proposition is to accept there is a differentiated benefit according to those in a similar economic situation or who can pay more or those who receive greater benefits; it is the use of differentiation in the levy that is evidence of some nexus.

In the United States, impact fees completely unrelated to any benefit as detached from the location are said to be “so controversial and so subject to legal attack” (Rosenberg 2005, p. 206). It is controversial because it is payment for off-site infrastructure not related to a project but related to a more general system. It can be justified obliquely in many ways, such as harm minimisation to prevent the adverse effects of future development without infrastructure, for the community to fund infrastructure in order to be responsible for increased population and housing without which the existing infrastructure would be congested, as allowing synchronisation of infrastructure with housing, as relieving the government’s need to access debt, and,

most importantly, that these fees are a means to align private interests with social objectives.

These comments, found in various forms in the extensive literature on the efficacy of system-wide value capture, do not actually address the point at which the levy is completely unrelated to any benefit, changing it from an understandable contribution to a tax. As well, there is no recognition of the relative benefits received and the amount of the levy in any Australian system. The reason for this is that, when looked at from a need to fund infrastructure, the important quality is to obtain the funds most efficiently. To start adjusting each levy according the relative benefit lacks efficiency. Nevertheless, there is no philosophical or historic basis for requiring a levy on those who have no stake in what is being provided, otherwise than as a tax.

The Method of Differential Valuation

In order to establish those who receive a benefit from infrastructure and those who do not, it is necessary to indicate the basis of such an analysis. Benefit cannot be measured in the abstract but only in terms of the effect on value. If it is measured without an objective indicator, it will take into account a landowner's proclivity to use a service, different ages of occupants, health considerations, and the myriad of other issues that lead to a subjective or qualitative analysis. Value is the measure of benefit from infrastructure only because a base can be established on known criteria assessed for accessibility effects.

The value of land for the purpose of measuring benefit effects consist of three aspects of the capitalised value: the urban externalities of location and natural amenities, the social infrastructure such as schools, hospitals and other public services, and the development infrastructure that already exists, such as sewerage collection and transport systems (Fensham & Gleeson 2003). Infrastructure may have differing effects on each of the three aspects: a bus lane will have a direct impact on access to social infrastructure such as a hospital but an indirect effect on sewerage collection. It is necessary to proceed in this manner because there cannot be said that any particular form of infrastructure has a linear effect on every aspect of

value; for instance, a recent study of rapid bus lanes in Brisbane found that proximity to bus lanes increase value more than proximity to train stations (Mully, et. al 2016). A standard pricing model reflecting the land market can then be applied to see what the increase in value will be and at what point there is no longer a benefit observable. This tripartite model is necessary because of the economic assessment for land value as a general concept because, for instance in the case of transportation, preferences may change depending on cost (Arnott and Stiglitz 1981).

Accessibility to infrastructure has been analysed most in the case of transportation. In that research, the two components of the cost of travel, determined by the spatial distribution of travelers and travel opportunities as well as the quality and quantity of opportunities, has been used to analyse supply and demand issues (Paez, Scott & Morency 2012). For an overall method to establish the value effect and therefore the benefit of infrastructure, hedonic price theory provides some answers.

Hedonic price theory values the effect of urban public goods. The value of the land is analysed according, in the case of transport infrastructure, to proximity to an urban railway station based on walking distance, the proximity to different levels of the competitive mobility options such as levels of the road network: a motorway, radial network, and local distribution roads, and finally the proximity to larger commuter networks based again on walking distance. Value is then ascertained by market price broken down by the attributes of the property, such as bedrooms and garage, neighbourhood attributes, such as educational levels and shopping, and the accessibility attributes to see the variation depending on the later variable for those values that are comparable for the other two (Martinez & Viegas 2012).

The hedonic theory offers a regression model to determine the differential location variables or the benefit derived from the supply of public goods. In 2013, hedonic pricing was applied to determine the effect of rail on metropolitan Perth (McIntosh & Trubka 2013). The study used a complete data set to analyse 462,476 residential dwellings, 6,322 commercial, and 8,243 industrial parcels to determine the per square metre land values. Sixteen variables related to base value were modelled, such as distance to the CBD. Twenty-eight models were then applied for each land

use. The hedonic models then produced results according to the percentage that property values would change because of location variables. The results are explained for residential values as:

> "The metropolitan-wide model estimated 14% uplift of properties within 400 metres walking distance of a train station, dropping to 12% for properties between 400 and 800 metres of a train station and then to a meagre 1% uplift for those between 800 and 1600 metres, which are consistent with other international studies" (p. 7).

Another study used hedonic pricing to determine the effect of Sydney's key transit routes and transit oriented design urban renewal (LUTI 2016). The study examined the effect on land values of heavy rail, main roads, rezoning, and increasing development density in terms of Floor Space Ratios. In terms of heavy rail, the findings, consistent with the Perth study, was that property within 0-400 metres had a 4.5% uplift in value, that within 400-800 metres had a 1.3% increase and those within 800-1600 metres derived a 0.3% rise. Those within 0-100 metres of a main road suffered a -7.6% loss.

The Sydney study examined the results of the hedonic modelling in terms of value capture possibilities. It is here that the study obscured the distinctions between a direct benefit and land which does not derive benefits. This is important to investigate as it is the basis for many value capture mechanisms or arguments as to methods to be used. The study maintains that the land market prices monetise land transit infrastructure at the start but that this has an expansion effect on the catchment. It asserts that "The demand for access to catchments drives land use change to capitalise on the benefits that the investment has created" (p. 17). The report concludes:

> "When the land value impacts of improving transit accessibility, rezoning land to its highest and best use, and increasing FSR to allow greater densities are considered in combination, the value growth potential is substantial and forms the basis for value capture strategies" (p. 100).

It is clear in both studies that the public good analysed for rail does not benefit all members of the catchment in the same manner and in fact the benefit decreases rapidly as distance from the station increases. The unwarranted leap in the Sydney study is that the existence of rail will attract rezoning and that in turn will lead to higher density increasing the value of land in the entire catchment. The infrastructure itself is considered the proximate cause of the land value as it starts a chain of events that results in an uplift in value. For those who have no nexus with the transit infrastructure, the benefit would come by granting them an unearned increment by betterment theory. That could occur at the same time as the transit but, as the study suggests, it follows later or, as a matter of planning practice, the area is rezoned based on future train stations or other areas. The infrastructure has a ripple effect and that is the basis for a levy for those that do not directly benefit from the fact of the infrastructure. This is perhaps the basis for development levies that mix in betterment as in Queensland, even though not made explicit.

The sequence in the Study is not necessarily correct. The designation of a growth area prior to infrastructure is the logical first step in strategic planning. An area is examined as having the capacity to absorb population and then it is designated as an actual growth area as are other areas. The sequencing of areas is what triggers the activity. Until a growth area is “switched on,” it is unlikely to be a magnet for development. On the other hand, forward commitments from transit authorities are based on a twenty or thirty-year demand analyses; infrastructure may in fact come before choosing an area for growth, but it is unlikely. However, when it does precede the selection of growth areas, a recent comparative research study indicates that not all infrastructure had the same effect. The provision of a road network is much more significant than rail in leading to growth and for rail, its impact depends on prior development leading to accessibility (Kasraian, Matt, Stead & van Wee 2016).

A classic analysis of the effect of transport on growth concludes is that it only has effect on values and economic growth as a complement to three other factors: a good quality labor force, availability of funds for investment in the area, and choices made politically to foster development (Banister & Berechman 2000). This suggests for transport infrastructure that the growth must exist first. For roads, it may be that

the growth will follow. For either form of infrastructure, the political will manifested by land use choices is necessary as well as the ability to create growth through development.

It is not therefore possible to assert that all infrastructure will result in a change in zoning that in turn adds value to land. In the list of infrastructure requirements for the growth areas in New South Wales, appearing in the *Environmental Planning and Assessment (Special Infrastructure Contribution – Western Sydney Growth Areas) Determination 2011,* the infrastructure listed is: roads, rail, bus, education, health, emergency, open space and conservation, planning and delivery. All of these vary in effect. The planning and delivery is not strictly an infrastructure cost but rather it is an operational cost of precinct planning for the area. Precinct planning is related to specific detail within the growth areas to lead to an indicative plan for land uses. In terms of nexus, it might be said to coordinate development and timing related to infrastructure commitments and therefore has some role to play in infrastructure.

It is useful to briefly return to the legal decisions that reasoned through the concept of an indirect benefit to see if they can be somehow interpreted to accept a levy based on this loose connection derived from the analysis of indirect benefit. In *Dogild Pty Ltd v Warringah Council* [2008] NSWLEC 53; (2008) 158 LGERA 429, a condition was imposed on development consent that the applicant provide a right of way on the rear lane. The requirement was clear that the condition "must fairly and reasonably relate to the development." The *Newbury* tests that propounded this aspect of validity of a condition, were said to be in addition to any requirement in a statute and therefore a tenet of common law. It is clear in other decisions that what is fair and reasonable depends on the circumstances. However, Stein J. *in Parramatta City Council v Peterson* (1987) 61 LGRA 286, went further and stated:

> "In my opinion the second test of whether the condition fairly and reasonably relates to the permitted development is not answered simply by geographical proximity but rather whether the development is benefited by the public amenity provided. There is no doubt that it must benefit, (as indeed will the Parramatta CBD as a whole), even though the benefit may not be a direct one (in terms of geographical proximity)" (p. 296).

No longer was a direct connection necessary, according to this statement, but rather the test included a broad view of that connection as long as there was a benefit to the development of some sort. However, in *Dogild,* it was found that there was insufficient benefit; in fact, a detriment, in relation to what was being proposed. There had to be some *benefit* for the condition to be valid, even if indirect or remote geographically, which was offset by a detriment so that the development overall is not benefited by the condition.

This loose nexus between zoning, value creation, and infrastructure embraced in an infrastructure contribution levy is generalised and does not accord with the idea that there be a specific benefit flowing to a landowner by a nexus with infrastructure resulting in exchange value. For those who receive immediate benefit, the nexus is there; for those who may receive some benefit by the area's development raising land values, the nexus is remote and may turn into a detriment. This arrangement seems to be the norm in indirect value capture across several countries. An analysis of value capture tools explained their proliferation:

> "As counterintuitive as it may seem … these instruments – with their 'messy' rationales and exposure to legal challenges – hold the most realistic potential for funding public services rather than their elegant direct-capture siblings" (Alterman 2012, p. 776).

However, it must be recognised that these devices offend the need for a discoverable nexus between the development and infrastructure and fail as a source of exchange value. They establish a weak connection in certain cases where the owner receives no benefit and then apply a betterment levy, disguised as exchange value. The circumstances of an infrastructure contribution require that certain owners pay a levy as a condition of development consent without receiving any ascertainable benefit, except that there will be infrastructure in the future. As it is not possible to conclude that the increase in land value by zoning is the basis of a levy as a betterment tax, then the test is only if the benefit can be found within a circumstance that vaguely suggests an exchange is to come.

The principle of nexus is established to limit the discretion of the planning authority that could otherwise impose any condition it deems fit. There is no basis for ignoring the nexus as a touchstone for levies as infrastructure placement has different effects verified by hedonic pricing in a single catchment. The uplift in zoning is not related to infrastructure and generates unearned increments and can be the subject of a tax. To mix the two is confusing and distorts the principle upon which infrastructure funding should be grounded.

Proportionate Sharing

If the starting point for an investigation into the efficacy of infrastructure contributions is the need for a rational nexus between the levy and the service, it is not possible to prove the connection in many cases. Marginal cost pricing suggests that those who give rise to new growth are the ones that must bear the costs as they are necessitating infrastructure. If an area is opened up for development as a growth area, it does not necessarily require infrastructure unless the land is in fact utilised. A developer who decides to subdivide a large area and erect housing is creating the need for new infrastructure, not as a direct externality, but by enlivening the growth of the entire area. According to marginal cost pricing, the existing owners of land not yet developed should not subsidise the developer's initiatives. An infrastructure contribution levy is therefore the logical means to shift the burden to those who have created the need.

The essence of "need" is that there is a nexus and thus the costs must be allocated to those who actually create that requirement. The difficulty is that infrastructure provision is, as the term is often used, "lumpy:" some developments require a new road as soon as possible and other infrastructure may come later, meaning a future developer has not been advantaged by the new road but may need to have other infrastructure that, given the time elapsed, may be more expensive. There needs to be a manner then of "allowing for the time-price differential inherent in fair comparisons of amounts paid at different times" (Nelson, Bowles, Jurgensmeyer & Nicholas 2008).

The methodology for allocating contribution fees over time and over benefit must postulate that the infrastructure provides the same internal rate of return over the life of the investment, as it represents the present value of the investment and the present value of the future benefits. The future benefit flows cannot however be calculated as they cannot be estimated and may be intangible. It is therefore difficult to understand how the levy is annuitised over the economic life of the project. Models that have emerged for proportionate benefit have suggested ways to account for the timing of development even when future benefits are impossible to measure but they are too complicated for application (Cox & Followill 2012).

The conclusion that follows is that the use of hedonic price theory or a model for calculating proportionate sharing is not practically possible in the administration of a levy. This means that the nexus has to be accepted as wide and based on marginal pricing as arising from activities of the developer.

Point of Incidence

Under the New South Wales *Special Infrastructure Contribution Determination of 2011*, when a landowner obtains development consent, the levy is payable before a Construction Certificate is issued. If a Construction Certificate is not needed, the contribution is to be made before any work is commenced on the land. A Construction Certificate is issued by a private certifier or consent authority and is used to indicate the work complies with the *Building Code of Australia*, and the plans are consistent with the consent. For subdivision approval, the levy must be paid before a subdivision certificate is issued. There is a provision for deferred payment if the landowner executes a deed of charge over the land at which time a caveat will be lodged or otherwise be secured by a bank guarantee. At that point, the deferred payment must be made within 3 years from the date of issue of the subdivision certificate. The original requirement for subdivisions in a 2008 Practice Note gave no opportunity for deferral.

With some exceptions, the contribution applies to all development in the Growth Centres and the contribution is imposed as a specific condition of development

consent under a 2011 Ministerial Direction to councils. Development consent and subdivision approval are the triggering events as the rationale is that the value is created at that stage. This is because the approval runs with the land and benefits subsequent purchasers, meaning the value has been increased as it is manifested. It does not occur on full realisation of the value, as when the development is created or the subdivided lots are sold.

In Victoria, the Growth Areas Infrastructure Contribution scheme of 2010 provides for trigger events for payment upon settlement for a sale of land, the subdivision of land upon a statement of compliance with conditions, and receipt of a building permit. The duty falls upon the purchaser or any corporation that makes a significant acquisition of interest in the land to make the payment within 3 months of settlement. On subdivision, the landowner with approval pays the levy within 3 months after the statement of compliance and before registration for titles. An application for a building permit triggers a duty on the landowner to pay before the permit is issued. The levy is only on the "first" triggering event.

In Queensland, payment is triggered by a material change of use payable on the endorsement of a building plan and commencement of the use, and reconfiguration of a lot (subdivision) prior to the endorsement of the plan of subdivision. The material change of use is another way of using development consent as the point of incidence because the concept of development includes both physical development and a change of use. If land is rezoned to a higher use, an application to change the use is necessary.

The effect of crystallising value at the time of consent in New South Wales has the effect of paying for value that has not been realised, causing the landowner to finance the levy prior to receiving a profit resulting from the placement of infrastructure. The justification is that the land is now of greater value as the consent will run with the land. However, the development consent lapses in 5 years (by Section 95 of the *Environmental Planning and Assessment Act*) and that period could be reduced by the consent authority. The consent does not lapse if a building is erected or there are lots created in a subdivision or work has commenced to a certain degree. Accordingly, if a landowner receives consent, it is possible that after

payment of the levy there may be difficulty financing development and the consent will lapse, meaning there is a payment without any realisation. The concept in Victoria that the levy is paid for subdivision upon sale is a recognition that value is realised not just created. As well, the payment prior to a building permit brings the landowner closer to realisation and is evidence of an intention to build and develop.

The justification for using development consent as the point of incidence is it is a point in time that is specific as opposed to the eventual realisation, which is in the future. The fixing of a time removes uncertainty, which affects investment decisions. The determination of value at the time of creation and not realisation is also justified because of the continuity of development consent and subdivision approval. A developer purchasing land with development consent is buying land for which the price will directly reflect the levy on the reasoning that the land is now more valuable because it can be used to realise value. However, if the land had not yet received development consent but has been earmarked for higher uses, such as land designated for high-rise development in a growth area, the developer may receive a higher price without the need to pay an exaction. The developer is getting an unearned increment that is not being levied but is still being realised in the price. From the period of the new zoning or land designation for higher uses until the development consent is given, there may be several land owners that reap the benefit that is clearly passed on to the eventual successful applicant for development consent. The planning gain is not taxed with a development levy because the point of incidence requires a triggering event.

In the case of Victoria, which has not tied the levy to the specifics of infrastructure, the point of incidence means that it is a betterment levy, capturing value on sale to be paid by the purchaser. The triggering events of development consent or subdivision approval can be earlier or later in time to sale. If they are earlier, the justification for the levy is not grounded in any form of nexus with infrastructure and the betterment charge may be capturing only a small amount of what is a future uplift on sale. If they are later, the sale does not capture the eventual refinement of the area by detailed plans and the possible greater increase in value.

The impact of infrastructure contributions on developers means that the fees will be somehow distributed among future owners and tenants. In fact, the levy can be absorbed by a developer who is willing to accept less profit or "passed back" or by buying land cheaper, or "passed on" to future purchasers. The pass on effect was one of the early reasons that there was some acceptance of these levies in the United States (Huffman, Nelson, Smith & Stegman 1988), on the basis that the burden was manageable if it was spread wider. In that case, it does not matter when the burden is created, aside from the carrying charges for increased funding requirements. Research is tending to the view that the effect of the contributions is to "pass on" the cost in an increase in house prices (Lyndall 2015; Murray 2016).

The activities of developers are not consistent so some may redesign the cost of a project to recoup a levy and others may simply wait because they cannot reach the right profit level, are unable to receive finance, or let time pass to realise general property inflation. Experience in the UK and Australia with betterment levies shows that the cost may be too high and this will affect the development supply chain. It is likely, although not proven conclusively, that this may be the case with development contributions to some extent.

The Effect of the Triggering Event

If infrastructure is built in an area, everyone will reap some benefit. Proximity to a railway station for existing uses will undeniably increase value. When the triggering event is development consent and subdivision approval, the contribution levy becomes a crude form of betterment. The consent and approval are indications that the value that was created or will be created by the infrastructure has now been enhanced. This is providing a further uplift in value by the operation of the planning system, the key ingredient of a betterment levy. The system hides the betterment effect by relating the payment to a point of incidence that appears convenient and identifiable. However, these events are related to obtaining a benefit from the system and it is at that point the payment is made.

When the payment is on a sale and thus the recovery of value falls to the purchaser, this also a recognition that the land value has fixed. In this case, it can be said that it

is not fixed because of the planning system but rather because the land was benefited by the infrastructure. When payment is on the acquisition of land by a consortium, that too can be traced to a nexus.

The confusion comes from fitting in methods of value capture reliant upon the planning system and its devices. If there are obvious tools for marking value creation – development consent and subdivision – than the manner of collection has the advantage of being clear. However, the unseen effect is to change the infrastructure system into a betterment levy as it is not only capturing the uplift from the consent or approval but also that which has already crystallised by the demarcation of the area for growth.

Negotiated Contribution Levies

Section 94 of the New South Wales *Environmental and Planning Assessment Act* has a long history since it was introduced. The purpose of the Section was to codify the manner in which developers of land had to contribute to local authorities for off-site infrastructure resulting from their developments. The Simpson Inquiry of 1989 suggested that a local council prepare a development contribution plan to indicate what infrastructure is needed within the local authority and to establish a nexus between development and the need for contributions.

A series of unconvincing articles from 1991 to 1998 suggested that there be a means of collective bargaining as to the extent of these contributions. The arguments, which lacked cogency or any theoretical underpinning, were based entirely upon speed, certainty, and expanding the range of approaches (Taylor 1991; 1997; 1998). The success of the UK system of "planning obligations" was called into aid to promote negotiation of development charges. There has been particular success in the UK in providing affordable housing through the use of negotiated agreements (Rowly, Crook, Hennebery & Whitehead 2015). The UK system, however, had vastly different antecedents including a history of negotiation during the process of a development applications. As well, social housing in the UK was originally organised to be placed on land that had little opportunity for development and where there was

difficulty in developers agreeing to allocate development land for such use. As the need for affordable housing continued, the UK *Town and Country Planning Act 1990* was amended to bring this need for contributions into the decision-making process. However, there was a difficulty conceptually to get developers to give up land where there was no connection with the development. For that reason, negotiation was an option when there was a nexus.

Section 94 was not suited for growth areas that extended over multiple local government areas and was not useful for areas of slow urban growth where developers were inactive in seeking consent. In 2005, two changes were made that removed the need for a nexus. The first was that a Planning Agreement could be entered into for funding infrastructure and (Section 93F(4)) "A provision of a planning agreement in respect of development is not invalid by reason only that there is no connection between the development and the object of expenditure of any money required to be paid by the provision." The second (Section 94A) was the introduction of a fixed levy over all development in an area again with the caveat that no nexus needed to be found.

The new provisions were added in 2005 by then Minister Knowles in a period where the Sydney Metropolitan Strategy had reached fruition and there was no governance structure in place for its implementation. The Minister had set up the Section 94 Contribution and Development Levies Taskforce that recommended development agreements were particularly useful for growth areas as there was no other mechanism in place that appeared effective.

The "Voluntary Planning Agreement" that provides for negotiated contributions is used in two situations: when the applicant seeks a rezoning or a development consent. VPAs have been used in growth areas, such as for the Elderslie and Spring Farm release areas. These agreements are not able to be appealed to the Land and Environment Court, meaning their content can be wider than any condition requiring a nexus between the development and the infrastructure. As the definition of what is covered is so wide, the landowner is negotiating for a privilege, even though the provisions are clear that the Agreement cannot guarantee a rezoning or development consent.

The effect of the VPA, bolstered by the weak series of articles expounding the benefits of the UK system, is to provide for a levy when the landowner is seeking an uplift in value by rezoning or consent. As it does not require a nexus with specific infrastructure, the only reasoning can be that it is imposing a form of betterment levy, as that is functionally defined as obtaining a percentage of value from the operation of the planning system. This was perhaps understood when VPAs were introduced. The *Development Contributions Practice Note* in 2005 contains this confusing statement:

> "Planning benefits. The provision of planning benefits for the wider community through planning agreements necessarily involves capturing part of development profit for that purpose. The value of planning benefits should always be restricted to a reasonable share of development profit. Planning benefits should never be obtained through planning agreements as a form of taxation on development. Accordingly, planning benefits, though primarily directed to the wider community, must never be wholly un-related to development contributing the benefit."

This major shift from Section 94 that required a nexus to a VPA that does not and Section 94A that also does not require such a connection is not readily explicable. The Taskforce had recommended the continuation of a nexus. The Second Reading speech on behalf of Mr Knowles suggests that this open negotiation was perceived as an accepted on-going practice and this would merely establish a framework for what already exists (Hansard 8/12/2004). It was also added:

> "The State Government can be a party to, and receive contributions under, an agreement. In order to provide for flexible outcomes that best serve the public interest, there does not have to be a direct nexus or connection between development to which a planning agreement relates and the object of expenditure of any money required to be paid under the agreement."

At this time, there was no Australian precedent for removing the nexus test to provide for a betterment form of levy. In Victoria, for example, Section 173 agreements merely facilitated making agreements but did not widen the scope of the

nexus for a contribution levy. There are several possibilities as a matter of conjecture as it needs to be pondered as to why such a momentous change went unnoticed. It could have been a reaction to the need for the massive Metropolitan Strategy infrastructure that could not be covered by a nexus test or the inclusion of infrastructure that had not previously been caught by infrastructure levies. In fact, the Special Infrastructure Contribution Determination included Education, a public service that would only benefit some. In any event, it represents a major shift from the essence of Section 94 but its most detrimental effect has been that it has unleashed unrestricted betterment charges for local authorities.

The City of Leichhardt, now part of the Inner West Council, developed the *Voluntary Planning Agreements Policy* in 2015 that provides (para 36.12) that Council "will generally seek 50% of the uplift value…" The basis of the uplift is the pre-VPA value and the post-VPA change in the zoning. This is now the norm for many Council policies under the rubric of planning agreements. This constitutes an unexamined major policy shift introducing a system of betterment charges to operate in addition to a contribution made through establishing a nexus.

The rationale for planning obligations in the UK, removed from the need for a nexus, was a deliberate political determination in light of the history of capturing planning gain and for a need for social housing. Section 106 established a legislative scheme to create an agreement as to the impacts of the development on the wider community and betterment capture re-emerged as a relevant fit. As the focus was on the material considerations in granting a consent and not on a development plan, which at most offered guidance, the idea of collective bargaining for the development rights was part of the fabric of that planning regime.

The justification of a betterment levy in New South Wales founded on the removal of the nexus arises in the context of no deliberate political imperative, no history of success for betterment levies, and differs in operation and history from the UK as uplift arising from rezoning does not exist in that system. If a VPA system of betterment is to be used, it needs to be accomplished by specific legislative intent.

Capacity to Pay

The Draft Woollahra *Voluntary Planning Agreement Policy* provides an explicit formula for betterment capture in similar, more fulsome terms but adds the following: (para 4.3):

> "The Council will seek opportunities to negotiate a planning agreement which includes a land value capture component. In negotiating such an agreement, the affect (sic) on the economic viability of the proposed development will be an important consideration in establishing the amount of development contribution or whether the agreement will contain a land value capture component."

The idea of assessing the economic viability and the capacity of the developer to pay has its origins in the concept of "sustainability." The UK *National Planning Policy Framework* (NPPF) explains (para 173):

> "Pursuing sustainable development requires careful attention to viability and costs in plan-making and decision-taking. Plans should be deliverable. Therefore, the sites and the scale of development identified in the plan should not be subject to such a scale of obligations and policy burdens that their ability to be developed viably is threatened."

The UK *National Planning Practice Guidance 2014* provides that, in terms of planning obligations, viability is important to make sure there are "realistic decisions" that support economic growth. The NPPF explains viability in terms of providing "competitive returns" to enable the development to be "deliverable." Various formulae have been used, such as the "Three Dragons Toolkit" for the effect of providing affordable housing. The Toolkit has default house prices by area, build costs, and affordable housing costs.

Most models use a 20% profit as the standard measure but some use a perhaps more realistic view of 12-15%. However, the difference in the input of variables very much affects the outcome of what is viable. As such, the determination of viability

has been characterised as a weak process that is lacking any clear governance model (McAllister, Street & Wyatt 2016).

The factors that led to a consideration of viability were not that the burden was too great on the developer and that it would be unfair to require an exaction but rather that the planning system cannot fail to deliver economic growth. Accordingly, the effect on the developer is of interest in a wider community framework. This is the case especially if a betterment levy is added to an infrastructure contribution. In the case of large projects with specific rezonings and therefore massive uplift, the combined exactions can result in a loss of the facility to the community or a significant delay.

Timing of Recovery

Infrastructure needs are fixed at the time of creation of a growth area. The entirety of infrastructure then needed over time is aggregated into a central list of future requirements. From the time the list is settled, the priority areas may be years from being developed. In many cases, because of the fact that there are large land holdings in the hands of one developer, that area may leapfrog others and development may be accelerated. Infrastructure may be developed in original growth areas over decades. In the case of New South Wales, only some of the areas earmarked as priority growth areas have been developed after eleven years from the time of their designation. Others are not underway or are awaiting precinct planning for tighter analysis of the urban form.

The consequence of delays for development is slow payment of infrastructure contributions. Some areas begin to fill up and yield development or subdivision applications. At that point, some payments come in but there is always a significant lag between financing the cost of infrastructure and receiving the needed funding. More importantly, when *some* of the land is developed, the potential for value capture is not realised because the value is not unlocked unless there is an application for development. In areas where there are pre-existing agricultural uses or land is not able to be developed because of environmental constraints or lack of landowner viability, the levy may never be collected even though the infrastructure

must be built. The effect is that the formula of calculating the total infrastructure need and dividing it by the developable area will always be lacking in its effectiveness.

Government Cooperation for Unlocking Value

Infrastructure Contributions are dependent upon the point of incidence: development consent or subdivision approval. It may be that a landowner is unable to create any development opportunities because the land holding is fragmented, unsuited as contaminated or environmentally sensitive, or the landowner does not have the means or inclination.

Cooperative arrangements between the planning authority and landowners can create development opportunities where there may be limitations. An advantage of cooperation is that the level of eventual funding can be better calculated as development opportunities can be assessed from the beginning. As part of negotiations and cooperation, the examination of complex issues of feasibility, highest and best use, timing of development and finance can be evaluated.   The advantages of these arrangements that can be applied to value creation and value realisation are:

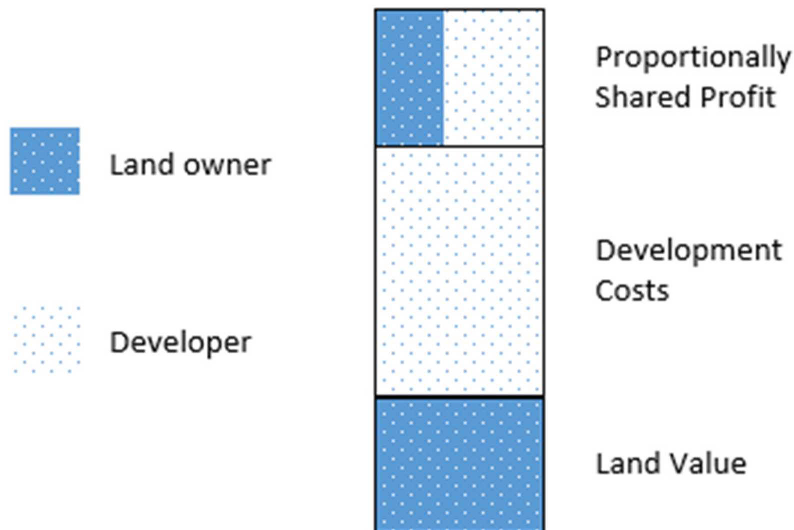
- They can accelerate both value creation and realisation, bringing development on stream in advance of its eventual development cycle;
- They can provide for accurate feasibility forecasting and timing of funding;
- They can reduce risks to government of not receiving the value capture;
- They can improve integration of planning with transport and local planning agendas by exploiting appropriate place-based development possibilities;
- They can create cooperative participation of the community in transport decisions.

Value creation, although the basis for a levy, does not alone result in benefits to landowners. Ideally, there must also be value realisation that manifests the created value in a manner that can absorb an infrastructure levy. However, even though the cooperative venture is based on creation as well as realisation, value creation is the

main focus for an infrastructure levy because value realisation in a cooperative arrangement, but, although ideal, is not practical. For a public body to be concerned with value realisation, it would have to be involved in construction, marketing, and land transactions. This is appropriate only in some instances, where the land is ceded by government to an authority to sell off for profit or the authority buys land at a pre-developed price to sell later. There is a tradition in Australia for this type of arrangement, perhaps starting with the *Municipality of Fremantle Act 1925* that allowed the city to acquire land compulsorily on both sides of a new road and then sell off the lots at a profit to fund the works, and more recently with the Northwest Metro Project.

Although value realisation is the essence of a cooperative arrangement, it is not practical for an agency to be involved in the details of implementation. As well, from a legal standpoint, the value capture takes effect when the value is created by development permission, not on the basis of actualised profit. This should not be seen as a difficulty in the formation of a cooperative arrangement because the development consent *runs with the land* and the value is increased for the purpose of sale, thereby conferring on the owner a gain through cooperation.

The increase in value creation for a landowner not motivated or unable to make an application for development requires assistance by a public authority. The project roles and relationships appear to be of the consent authority and a landowner. However, there are really only two possible participants in a cooperative arrangement with the landowner. The first is a developer who can manifest a project. In areas where the opportunity creates an obvious possible high yield, the developer will work with the landowner to unlock potential value in a simple arrangement. A Western Australian study illustrates the manner in which this can occur (Curtin University 2015, p. 5):

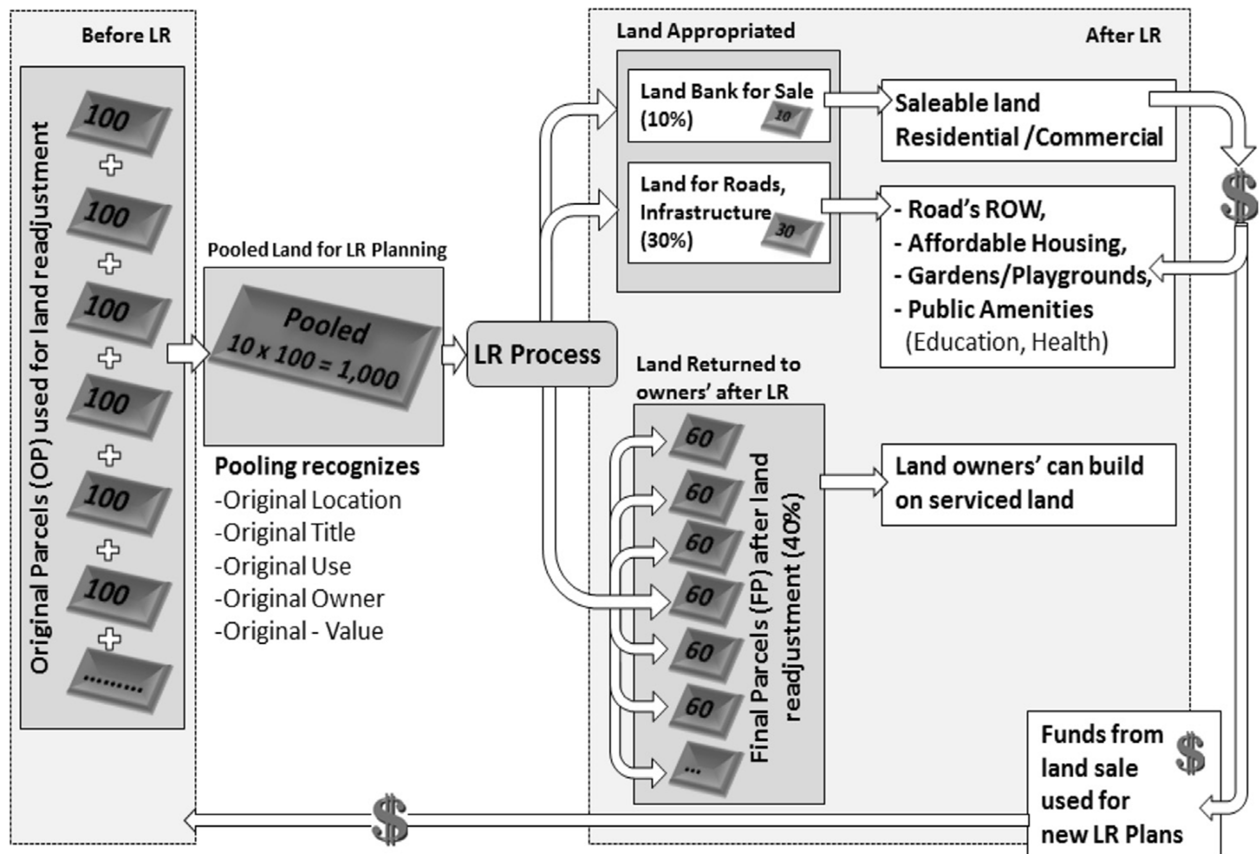


The study indicates that this is an "entrepreneurial model" where private funding is employed but does not preclude working with government for assistance in land assembly, grants of public land, or other efficiency gains. However, the respective roles are assigned to the developer and landowner outside the participation of government.

The relationship appears straightforward where the size of a project attracts a developer. However, as there are diverse holdings, some land in required for infrastructure may not readily be able to be developed due to environmental constraints, contamination, irregular lot sizes, subdivision restrictions, or the myriad of issues that confront exploitation of land. Where there are situations where there is no developer willing to seek a profit, this would require the state to enter into a cooperative arrangement with an owner or contiguous owners for the purpose of developing the land, pooling land where necessary, or, alternatively, acquiring land.

A technique that is used where there are irregular shaped lots, inaccessible land, or land that is environmentally sensitive, is land "readjustment." In this arrangement, land is pooled and then readjusted into parcels that are returned to owners, and some can be the subject of development and create value for all landowners. This has the advantage of inducing smaller land holders to develop, to overcome land ownerships that are not productive, and also to create a land bank, where some land

can be sold off to finance development costs. This process involves the preparation of a layout plan including the allocation of land for a transit corridor. This illustration from an article reporting on such a project in India (Mittal 2014, p. 316) explains the process:



The role of state in a cooperative arrangement would be to assist owners to manifest value and to obtain development consent in order to create value and, if possible, to allow value realisation. There may be situations where an infrastructure agency would want to take on some of these risks, such as ceding land to expand a highly developable parcel, or acquiring land by agreement and then selling at a profit. Each arrangement obviously requires a separate analysis of risk.

The multiplicity of optional funding methods creates different possible relationships. A 2016 World Bank study examined and rated 24 funding instruments for transport (Ardila-Gomez, A. & Ortegon-Sanchez, A. 2016, pp. 27-29), all of which would

create different relationships and operators. Joint Development, as expressed by cooperative arrangements to unlock value scored the *highest* for indirect funding. The ratings of Joint Development cooperative arrangements as the best method have a sound theoretical underpinning because unlocking land value is the most effective method of funding other than direct grants. This idea of bringing underused assets on stream is not new and was offered as a basis for funding around the world by a 2002 study by the World Bank as a key to future infrastructure funding:

> "There are opportunities for increasing transparency and revenues through public land auctions, for conducting land-asset inventories and strategic land asset management to free up underused assets for infrastructure finance, and for capturing for the public part of the gains in land values created by major urban infrastructure investments" (Peterson 2009, p.x).

In Australia, it is the case that the land market is characterised by discontinuous development, making the possibility of assessing value creation impossible in normal operation. However, the ability to unlock value by development consent will also encourage value realisation for owners, increasing the ability to pay, on the reasoning that there was no previous access to an uplift in value and from an economic point of view the landowner will receive a subsidy. This is not inconsistent with any ideological, historical or efficacy issues in this country.

The commitment to finance the work necessary for the owner to create value by development consent requires a full analysis of the elements of risk: technical feasibility, economic viability, creditworthiness, completion risk, operating risk, legal and policy risk, environmental risk, and political risk. Although this is complicated, the historic difficulty for an authority has always been to accurately estimate the true cost of unlocked value, raising the possibility of increasing the cost to other landowners beyond what was expected. Case study findings have been that, in the case of PPPs, the refusal of the authority to finance upfront investment often results in an eventual loss by the inability to share in future revenue flows (Engel, Fisher & Galetovic 2013). In the case of the cooperative arrangements proposed, the inability

to take the risk of upfront financing for value creation will result in a loss of contribution funding

Evaluation Criteria for Development Contributions

Ideology

The imposition of a contribution for externalities caused by or likely to be caused by a development is consistent with economic and planning theory. The externalities may be direct and capable of precise definition or may be indirect but reasonably connected to the size, nature, and type of development. The concept of strategic planning embraces a wide planning scale so that the effect of development can be considered in a broader context. If there is some connection, even if it is remote, this accords with contemporary views of planning as properly occurring in an area that transcends local government boundaries.

If there is no connection at all between the contribution required and the externalities, then it is an imposition of either a betterment levy or tax applied to a specific area that is not consistent with Australian norms. Historically in Australia, the basis for a contribution has been that it emerges from the need to internalise an externality; this is, as a matter of law, understood. It emerges in this form because the contribution arises as a condition of development consent and as the power to make conditions is not unconstrained, it is reasonable to require the condition be related to planning, be related to the development, and be reasonable. This is part of the common law of Australia and has been applied as I basis of assessment of conditions in addition to the requirements in Section 94.

In the United States, the "rational nexus" approach and proportionality tests prevail and unrelated or excessive contributions have little place in the planning regimes. The questions that are relevant are (Evans-Crowley 2006):

1. Is the impact of the new development linked to the need for public facilities?
2. Is the fee proportional?

3. Is there a reasonable connection between the use of fees and the benefits proposed by the new development?

The nexus and proportionality tests are grounded on the importance of property rights as inclusive of value. A landowner is entitled to keep the value of their property as much as protect it from being taken away without compensation. In the UK, the development control system has placed value creation as an act of the state in granting consent and the rights of landowners to value are only inchoate. In the U.S., a non-connected betterment tax arising from a lack of nexus or proportion is anathema to private property rights.

The only way to understand the shift away from value as a private property right and conditions as being bounded by rationality and nexus is the change of a view of planning from a system of spatial allocation of land uses to one which is market oriented. As the contribution schemes for wide areas are only recent, the move can be assumed as a product of a fiscal crises in financing infrastructure. However, it may go deeper than that and be a result that the complexities of growth planning having been taken out of the hands of local authorities and given to central, top-down planning authorities. This change means that the rationale of top-down authorities is the wide-area level resolution of problems that ignores individual local governments, forces them into the position of administering state agendas, and ignores the relationship a landowner has with a local authority.

As a matter of exchange value and benefit, the logic of infrastructure contributions requires at least some connection between the infrastructure and payment, even if it arises from a market oriented application of planning policy. There appears no justification on the basis of any policy to use development contributions where there is no nexus whatsoever. On this reasoning, the examination of the nexus must be actual and assumed in cases where there is a defined area with specific needs; it cannot be assumed beyond that level.

Fairness

The concepts of horizontal and vertical equity are acceptable in the analysis of infrastructure contributions. Horizontal equity refers to a direct connection between the contribution and the infrastructure provided – the nexus, while vertical equity is concerned with equity among those who are within the area for which a contribution is levied. The combination of both concepts leads to an analysis of what is fair in the circumstances in relation to infrastructure contributions. An analysis of horizontal and vertical equity suggests various methods to assure fairness (Nelson, Nicolas & Juergensmeyer 2009). The tests are:

Judicious Fee Exemptions: Exemptions for those not receiving benefit from the levy;

Varying Fees by land use: Levy varies according to the impact of the infrastructure on different land uses;

Vary Fees by intensity: vary by intensity of land use, such as basing it on a square metres;

Assess by Marginal Impact: Vary the fee by actual impact, such as being close to a train station or further away;

Individual infrastructure: Do not charge school construction costs on non-residential development or mix all infrastructure into one category;

Calculate the need: If a development generates a particular need for some developers but not others, such as open space for parking, charge that proportionately*;*

Develop Detailed Plans: Be specific about each infrastructure item the basis of the levy;

Track Fee Usage:	Examine that the fee is being used in a timely way and within a specified area and for the benefit of properties that have paid;
No Existing Deficiencies:	Fund only new infrastructure that arises from the needs of the development and do not use the levy to fix deficiencies;
Avoid Double Counting:	If infrastructure is already funded by council rates or some other levy, do not charge for it again;
Exempt smaller properties:	Exempt small lots that are not being used or minor structures;
Practical payment plan:	Allow fees to be paid in installments or at a later stage.

The rating of infrastructure contributions in New South Wales, Queensland, and Victoria according to these fairness criteria are:

	Victoria GAIC	*Qld*	*NSW*	*VPA NSW*
Exemptions:	No	No	No	No
Vary by Land Use	Yes	Yes	Yes	No
Vary by Intensity	Yes	Yes	No	No
Vary by Impact	No	No	No	No
Charge by type	No	No	No	No
According to Benefit	No	No	No	No
Detailed Plans	No	No	Yes	No
Fee Usage	No	No	No	No
No fund deficiencies	No	No	No	No
No Double Counting	Yes	Yes	Yes	No

Exempt Smaller	Yes	Yes	Yes	No
Practical Payment	Yes	Yes	No	No

Some of these go part way to achieving a goal not fully reflected in Yes or No. However, it can be seen that the NSW Voluntary Planning Agreement fails all tests of fairness. The other forms are deficient in the qualities of horizontal and equitable fairness.

Efficiency

Of the value capture methods, a development contribution is most efficient as it theoretically is regulating the cost of externalities. It is not related to an uplift in value seemingly caused by planning decisions where the increase arises from general economic factors and decisions extraneous to the landowner. Practically, the methods for value capture by development contribution are not efficient as they have adverse effects on the market in terms of distribution of costs. The lack of a true connection between benefit and infrastructure means that some owners are subsidising benefits enjoyed by others. Hedonic pricing would be a better system but its application is very complex and would make administration impossible.

The critical problem with the development contribution system is that in all cases it is an amalgam of different ideological constructs. In Queensland, it seeks to blend the uplift in value by designation of the area for growth with the actual infrastructure expenditure. In New South Wales, the system of Voluntary Planning Agreements allows the uplift to be captured as well as a contribution for infrastructure. In Victoria, the lack of an express purpose for the contributions means that the amount paid for levies are not able to be constructed from the cost of infrastructure alone.

Section 4 Land Taxation

Theory of Land Taxation

Land taxation is a pure user pays system when applied by a local government for the purpose of obtaining revenue to finance municipal services, such as sewerage. The nexus between the tax and the supply is manifest as the services are for the benefit of every landowner. There is a benefit difference between users depending on the intensity of activities but each landowner is receiving a service that is necessary for the use of their property.

At a state level, land taxation is a wealth tax that runs parallel to the capital gains tax exemption on residences, requiring tax to be paid on the value of the land when it is not used as a principle place of residence or is used for primary production. The funds raised at the state level go into a general pool of revenue and are not linked to specific benefits. State land tax, *as it presently exists*, is not a form of value capture to be used for infrastructure due to its purpose and exemptions.

The manner in which land tax is applied at the local authority level is that a budget indicates the required expenditure, the assessed base is considered according to a valuation, the taxable base, which is the assessed base less exemptions, is calculated, and a tax rate is applied. Its original purpose as a wealth tax to break up large land holdings is now lost but it is an Ad Valorem tax, now part of the traditional tax bases in Australia.

To best understand the theory of local property taxation as a source for value capture, it is necessary to distinguish a tax from a levy. A United States decision explains the distinction clearly (*McCarthy v. City of Leawood*, 257 Kan. 566, 581, 894 P.2d 836, 845 (Kan. 1995)):

> "A fee is not a revenue measure, but a means of compensating the government for the cost of offering and regulating the special service, benefit or privilege. Payment of the fee is voluntary—an

individual can avoid the charge by choosing not to take advantage of the service, benefit or privilege offered."

The statement that the fee is "voluntary" is a factor that distinguishes a fee from a tax. It means that the developer does not have to create value and contribute to infrastructure by carrying out a triggering event such as a sale or by obtaining development consent. For a tax, every resident must pay regardless. Another distinguishing factor is that the property tax is continuous, applying year after year and a levy is a one-off payment. As well, the infrastructure that is the basis for a levy is projected far into the future and that for property tax is directed at a yearly expenditure.

The property tax and infrastructure are congruent instruments (Fischel 2000), although a property tax is not regarded as a major source of infrastructure funding; it was estimated in one study that it captured only 12% of the increase in land values over a twelve-month period (Stillwell & Jordan 2005, p. 222). However, aside from the ability of an owner to avoid the levy by not developing, a tax and levy are theoretically the same as both imply exchange value for a government provided asset or service. If there is no connection between the levy or tax and the benefit derived, the revenue is not a property tax or an infrastructure contribution but rather a wealth or betterment tax.

Use of Property Taxes as a form of value capture

When the property value is assessed for rates at current market value, which necessarily includes land and improvements, the argument can be made that it results in underutilised land as more improvements mean more tax. This is the reason that a tax on only the value of land is the traditional form. As a consequence, the valuation of land as unimproved value does not necessarily reflect the benefit of infrastructure that could result in more intense uses. It does capture some of the unearned increment that may have been caused by planning decisions in terms of the residual value of the land. However, it is not a betterment tax as the full uplift related to the exploitation of the land is not captured when unimproved capital value is used.

Using New South Wales as an example, a local government can tax land by setting a rate to be paid based on unimproved capital value – the land without improvements (*Valuation of Land Act 1916*, Section 6A). The rate by the *Local Government Act 1993*, Section 501 can be made for services and administration in relation to water, sewerage, drainage, and waste management but not infrastructure. The Act provides that other services can be included in Regulations but none have. The Victorian *Local Government Act 1987* allows a council to set a differential rate by using capital *improved* value. This rate is used by most councils in Victoria and is referred to as Capital Investment Value. Again, the use of rates is limited to services but not to the funding of infrastructure. In Western Australia, the concept of Gross Rental Value is used being the rent a property would expect to get if rented to a tenant.

Any of these systems of valuation: unimproved value, capital improved vale, and gross rental value can be used as a mechanism for raising funding for the infrastructure if the rating system was expressly designed for that purpose. They are not levies but rather taxes as the relationship between infrastructure and the amount is specific and they apply to all even if the landowner does not seek a higher use.

Rates in certain cases have elements of a betterment tax and resemble the structure of a levy, even though there is a nexus. In the case of high-density dwellings in New South Wales, land is valued according to it being zoned for high density purposes or as used for high density and, as well, that is the highest and best use. (Valuer General's Policy No. 2 August 2014 "Valuation of high density residential land"). The direct comparable sales method of unimproved vacant land is used except in the case of situations where there are insufficient sales and then a hypothetical development scenario is used. The complex valuation method of hypothetical development examines the land as vacant with no development consent but examines the land for its highest and best use as the current use. However, the increase in value from a planning scheme or development consent is in fact already captured by a rate. The essence of high density residential value is that it is capturing the value resulting from the use of land having regard to the establishment of comparable sales evidence for properties with similar uses and the consequent

residual vacant land component. It is the planning system that is allowing the density. The same is true of commercial property using different methods. All of these methods rely upon examining land used for a planning purpose that has increased the value of the land and the rate is therefore capturing that value.

Rating cannot be used for infrastructure funding as it is presently constituted. In addition to the subject matter of rates being restricted to certain municipal services, rates are capped. In Victoria, rates were capped in 1995, lifted in 1997, the cap was scrapped in 1999, and now reintroduced as of 2015 as part of the "Fair Go Rates System." Rates are therefore not able to account for the infrastructure needs in addition to the revenue necessary for services, such as water and sewerage. A variation can be sought by a council from the Essential Services Commission for funding vital infrastructure and infrastructure renewal. As of June 2016, only rural councils have been able to raise above the cap, unrelated to infrastructure.

A distinct advantage of using additional rates for infrastructure, if the rating system so allowed, is that the tax fund does not relate the levy to specific infrastructure, negating the need for a proportional benefit to be found. As well, the methods of valuation and collection are in place. As it is at the coal face for ordinary owners, its use is a political issue as can be seen by changes in rate capping, and a great increase will be difficult to justify when the argument is made that developers are receiving a benefit that can be passed on, meaning general owners would suffer as developers would gain.

In a thorough study of value capture methods, the case is argued for reform of the tax regimes to provide a broad based land tax increased for the purpose of funding infrastructure (Stapleton & Fox 2016). One reason given is that it is on-going rather than a one-off contribution for a levy. It is suggested in that study that if this tax was introduced by the state, there would be double taxation as there is already rating. Accordingly, it is stated that the two be aggregated. A further study suggests that infrastructure contributions are more volatile and susceptible to economic conditions than rating, leading to a conclusion in favour of rating as a sound source of revenue (Koutifaris & Mangioni 2012).

The main difficulty with a broad-based tax relating to infrastructure is that there is a large discrepancy between those who receive advantages by direct benefit, such as proximity to a rail station, and those who have no connection, such as rural areas on the urban fringe. Relying on valuation methods, it approaches a form of betterment tax, dependent not on the supply of infrastructure but rather the increase in value by the planning system. Unlike betterment levies, however, it is not triggered by an event such as sale or development consent but rather is an ongoing cost to landowners and has the advantage of being amortised on a yearly basis.

Evaluation of Property Taxes for Infrastructure

A property tax is a user pays system. It is limited in its use in Australia by exemptions, caps, and political issues relating to local government autonomy and its unpopularity. It is currently levied at the local government level only in exchange for services, as state land tax provides owner-occupied exemptions. There is no reason that the owner-occupied exemption could be removed if the tax is used by the state to fund specific infrastructure.

The greatest advantage of a property tax is that it is well known and visible. Landowners accept property tax as an aspect of home ownership, even though it is not popular. There is no argument to be made that property is not a suitable base for taxation. It is also traditionally argued that a tax on property qualifies as progressive as wealthy people own more land. It is also regarded historically as efficient as no economic behaviour can avoid the tax.

A system of property tax is most congruent with a user pays system because it spreads the burden on an annual basis to those who will be advantaged in some way by the infrastructure. It does not require any triggering event by which it captures developers only and, as it is broader based, it removes the need for examination of the proportionate benefit of infrastructure. The user is paying for infrastructure but the benefits are reframed as of benefit to the community spread across a state or local government. This represents a shift from marginal cost pricing to community absorption of infrastructure costs.

The budgeting process can be made the subject of independent scrutiny and more importantly community participation where priorities can be agreed and infrastructure identified, thus reducing the loss of nexus. There is no requirement for estimating what is caused by the new development in terms of infrastructure, what is the reasonable proportion that should be paid, no need to separate out the betterment proportion from the infrastructure benefit, and no need to estimate future costs as the tax is recalculated periodically.

Section 5 Recommendations for Australian Value Capture

Recommendations as to Betterment Levies

A betterment levy, unrelated to specific recovery of infrastructure costs, has no basis in law, ideologically, or in planning theory. It is a revenue raising exercise that improperly uses planning as the basis for an unfair imposition. It fails to take into account the accretion in values caused by external factors unrelated to planning. The choice of a percentage or fee cannot be based on any relevant factor as it is disconnected with any known cost.

Recommendation for Infrastructure Development Contributions

The theory of user pays dictates that there be a nexus between the infrastructure to be provided and the contribution. That nexus is the basis for the internalisation of externalities, the establishment of Australian legal principles, and the more general notion of fairness. That principle can be widened when there is a connection with the area and the infrastructure that will be provided in the future. Ideally, it would be best if the proportion that each person must pay is reflected in the benefit received. However, practically that is not possible. The alternative is to base the exaction on variations in land use, a concept recognised in all states as reflecting the potential benefit.

The point of incidence at development consent or subdivision approval reconfigures the contribution into a betterment charge capturing the prior uplift as well as the uplift from the approvals. This works against the infrastructure contribution as a user pays system. As well, as the events are so clearly defined as occurring prior to the actual realisation of the uplift by sale, development or use, the burden on the developer is unreasonable having regard to the incipient nature of the development. If the point of incidence was changed to where the developer had substantial time to realise the approvals, then the connection between benefit and infrastructure would be more apparent.

Although it may seem convenient to lump together the unearned increment with the recovery of infrastructure costs, it delegitimises the efficacy and operation of value capture. The Queensland scheme is an example of blending two ideologically different systems in one levy. The recommendation follows that an infrastructure contribution, no matter when triggered, must be related *only* to a proportional distribution of costs, connected as far as possible to relative benefits; it should not be combined with a betterment charge.

The use of Section 94A and Voluntary Planning Agreements in New South Wales completely offends the nexus principle and has led to exactions that are not justified. In particular, VPA's are against all the relevant principles to evaluate a levy. They were perhaps introduced in New South Wales to obtain funds beyond that arising from a nexus, but in any event, have led to local government abuse by forcing developers into a VPA to capture random betterment.

As a matter of efficiency in terms of development costs and the market, the recovery of the contribution within a longer time period that allows for realistic exploitation of the consent or approval is necessary. The point of incidence is too precipitous in New South Wales, creating an unfair burden in terms of the timing of payment; this is not alleviated by a caveat or bank guarantee. The idea of an exaction on the sale of land in Victoria causes a lack of intergenerational equity, granting a windfall to a previous owner. The issues as to point of incidence can be cured by allowing flexible terms of payment related to some extent to value realisation.

The recommendations that follow are that development contributions should rely upon the nexus principle *without exception*, as the only sound basis economically, ideologically and legally for their existence. As a consequence, betterment levies should not be mixed with development contributions; as much as possible there should be a connection between the infrastructure and the exaction in actual cost terms, the indexation of any payment should be on actual inflationary causes, the landowner should be given time to realise profit to be able to pay, and most importantly, the contribution should be made clear by an enunciation of the infrastructure and its benefit.

Recommendations as to Property Tax

A broad based tax that applies to the state or a regional government derived from a recurrent cost of infrastructure is the most effective form of value capture. It is ideologically sound as a user pays system where the individual nexus is not necessary as the broad base implies a community need. It needs to be considered in light of local rating practice by either differentiating carefully the infrastructure and services involved or applying a discount for the state infrastructure levy where they overlap.

Section 6 Operational Choices for Value Capture

There appear to be two operational systems for effective value capture. These two systems are the closest to a sound ideological orientation, fairness, and efficiency. The key to both is expanding the tax base and a greater spread of costs over time.

Revised Development Contribution Framework

1. There should be no attempt at capturing the unearned increment from the planning system;
2. The contribution must be based entirely on provision of infrastructure;
3. The community should be involved by way of community participation methods in the evaluation of infrastructure choices;
4. The infrastructure list should be revised on a periodic basis;
5. The infrastructure list should only contain that which arises from new development and not be used to catch up on deficient infrastructure not related to development;
6. The cost of the infrastructure should not be indexed but recalculated on revision;
7. Each year, the use of fees in relation to the supply of infrastructure must be disclosed;
8. The levy should be calculated on the developable area;
9. Exemptions should be for land unsuitable for development and small lots;
10. An exemption for hardship should be reviewed for each applicant;
11. There should be an appeal for the contribution plan and for cases of hardship;
12. A cooperative development scheme should be introduced to broaden the base and unlock value.
13. Attention should be paid to previous contributions through local contribution schemes;
14. The point of incidence should only be development consent or subdivision approval;

15. A landowner should be given substantial time to pay the fee to allow for value realisation;
16. There should be no voluntary agreements that vary the contribution scheme.

Property Tax for Growth Infrastructure

1. The most effective way to fund infrastructure in Australia is a broad-based tax applying across a state;
2. To be effective, the land tax must remove exemptions as to owner-occupied property;
3. The infrastructure budget must be a matter of consultation with the public;
4. The infrastructure included is that for growth areas that have been designated as ripe and ready to develop;
5. The infrastructure cost must be reviewed on a periodic basis;
6. The value of the land to absorb the tax is based on unimproved capital value;
7. The hypothetical development method should not be applied to valuation for a property tax for infrastructure;
8. The tax should have few exemptions and should be across all land uses;

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