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SUBMISSION TO THE CITY OF MELBOURNE AFFORDABLE HOUSING STRATEGY

Introduction

The Property Council of Australia welcomes the opportunity to respond to the City of Melbourne Draft Affordable Housing Strategy (**Strategy**), endorsed by the Future Melbourne Committee on 3 March 2020.

We are concerned that the Strategy's mandatory, rather than incentivised, approach to the provision of affordable housing will not achieve the desired policy outcomes. Further, we hold fundamental concerns with the progression of an affordable housing strategy which is underpinned by economic analysis conducted in a pre-COVID-19 environment.

The Property Council acknowledges that housing plays a significant role in Victoria's social and economic prosperity, and the importance of stable secure housing has been highlighted by the ongoing coronavirus pandemic. It is well accepted that a lack of affordable housing can lead to homelessness, poor health and lower rates of employment and education.

Affordable housing requires the cooperation of both government and industry and must remain viable for all parties. Noting this, the Property Council supports a model that provides appropriate incentives to encourage the development of new affordable housing stock.

This approach, rather than a mandated approach as proposed in the Strategy, has the greatest potential to achieve the outcome that both government and industry desire – a significant increase in affordable housing throughout Victoria and specifically in the City of Melbourne.

About the Property Council

The Property Council of Australia is the leading advocate for Australia's property industry – the economy's largest sector and employer.

The Victorian Division represents more than 500 members across all aspects of the industry. Its members are architects, urban designers, town planners, builders, investors and developers.

The Property Council supports smarter planning, better infrastructure, sustainability, and globally competitive investment and tax settings which enable its members to make a lasting contribution to the economic prosperity and social well-being of Australians.

Overview

The Strategy tabled by the City of Melbourne identifies four priorities it seeks to implement to address Melbourne's affordable housing crisis:

1. Advocate for mandatory inclusionary zoning.
2. Develop affordable rental housing on City of Melbourne land.
3. Strengthen our internal affordable housing processes.
4. Advocate and partner for affordable housing.

The Property Council's submission focusses primarily on the issue of mandatory inclusionary zoning and its inappropriateness in many circumstances.

Affordable housing in a COVID-19 economy

The Property Council has serious concerns with the progression of an affordable housing strategy that is underpinned by analysis conducted in a pre-COVID-19 environment.

The City of Melbourne has acknowledged that COVID has changed the playing field of development and that post-COVID trends were not incorporated into the SGS report upon which the Strategy was based (as they had not occurred when the report was developed). When the facts change, the approach must change.

It is inappropriate to progress with the Strategy in the current economic environment. In Victoria and globally, we are not operating in a "business as usual" environment. We are experiencing great uncertainty and an economic downturn of historic proportions.

On 22 April, the Victorian Premier and Treasurer announced that economic modelling produced by the Department of Treasury and Finance showed that as a result of the pandemic:

- 270,000 jobs will be lost in Victoria by September
- Gross State Product (GSP) will reduce from \$226 billion to \$194 billion in the first half of the calendar year 2020; and
- A fall to property prices of 9 per cent is expected by the end of 2020.¹

At such an uncertain time, additional taxes in the form of mandatory inclusionary zoning will place new developments at significant risk. Without these new developments, far fewer affordable dwellings will be built, completely counter to the City of Melbourne's policy intent.

¹ <https://www.premier.vic.gov.au/new-modelling-confirms-hit-to-economy-unemployment-spike/>

In addition, the *Building Victoria's Recovery Taskforce* has flagged that it will explore affordable housing requirements for Victoria and strategies to address its projected need. With a state-based approach being considered it would be unreasonable for the City of Melbourne to finalise the Strategy in isolation.

Although we agree that the need for stable secure housing is critical – even more so, at a time of great uncertainty, the assumptions underpinning the ability of the private sector to support this initiative are fundamentally incorrect in the current climate.

Analysis and assumptions underpinning the Strategy

The quantity of required affordable housing and the mechanisms by which affordable housing can be delivered relies heavily on a report produced by SGS.² Prior to the COVID pandemic, the Property Council raised several concerns about the figures and assumptions relied upon in the *SGS City of Melbourne Housing Needs Analysis (SGS report)* background report.

We have formally requested the City of Melbourne make available the figures and assumptions relied upon by SGS. This request was rejected.

Without access to this information, it is not possible to undertake a thorough and independent analysis of the SGS report or the many assumptions relied upon. However, we raise the following concerns.

Methodology

The publicly available SGS report suggests that its analysis applied the following steps:³

1. Creating a generic Residual Land Value (**RLV**) model, populated with preliminary cost and revenue assumptions (sourced by SGS and reviewed by m3property).
2. Incorporating available land and density data from the Council's 'development capacity project' into the RLV model.
3. Mapping and spreadsheet analysis of potential development sites to determine the number and location of residential development projects that are theoretically viable.
4. Assessing the impact of affordable housing requirements on development project viability.
5. Determining what share of viable projects might be abandoned or deferred because of reduced residual land values versus the capitalised value of current rent streams

The analysis conducted is no longer relevant or reliable. In the current economic crisis, both revenue and cost assumptions will have changed materially. In turn, this will impact the number of viable projects (and the number of dwellings per project), as well as the timeframe by which those projects can be delivered.

One of the key assumptions in any model of this nature is the land value. Most developers use a highest and best use valuation which guides land sales. Earlier versions of this model did not appear to use this valuation. It is not possible to say precisely what method of valuation has been used in this model because of the reluctance by the City of Melbourne to release the assumptions material, however, unless the correct assumption is used, the model cannot reflect industry practice or predict market behaviour.

² Draft Affordable Housing Strategy, p 31

³ City of Melbourne Housing Needs Analysis, p 92

Assumption about demand

According to the SGS report, there is a "current aggregate need for social and affordable housing in the City of Melbourne of at least 9,436 units... Current supply, as measured by the stock of social housing, is around 3,970 units".⁴

This approach implies a deficiency in social and affordable housing infrastructure of around 5,500 units. This approach however fails to include any privately held stock that meets the criteria of "affordable". Hence, the assumption that current demand is 5,500 is inaccurate.

Assumptions about private sector capability

Section 2.6 of the SGS report states that the nominal acquisition cost of a new affordable housing dwelling is \$0.5 million per unit. Assuming the accuracy of that statement, it is unrealistic to assume such a cost could be absorbed by the private sector without significant risk to the feasibility of a project.

Further, the SGS report acknowledges that, "some landowners will suffer a loss of value in their property,"⁵ if an inclusionary zoning target is introduced. Given that modelling by the Department of Treasury and Finance suggests that the value of property will fall by 9 per cent this calendar year, any further price falls (and resultant reduction in wealth accrued by residents of the City of Melbourne and often acquired as a retirement nest egg) created deliberately by way of local government policy is completely inappropriate.

Applying the existing assumptions, the SGS report highlights that "a ten percent affordable housing requirement reduces the number of feasible sites from 494 to 404 – an 18% reduction. This in turn reduces the number of feasible dwellings from 116,500 to 103,400 – a 16% reduction".⁶ This will be exacerbated by any national economic retraction associated with the post COVID-19 period.

Advocate for mandatory inclusionary zoning

The Property Council opposes the City of Melbourne's proposal to advocate to State Government for the introduction of mandatory inclusionary zoning on private land and, in particular, the proposition that mandatory inclusionary zoning should be applied to multiple land-use types including residential, commercial and industrial land.

We recognise that the provision of appropriate levels of affordable housing is reliant on several complex policy and market factors. It is not realistic to expect this issue to be solved by the property development industry alone, particularly given chronic and repeated under-investment in social housing by successive State and Federal governments and the issue of affordable housing being one which governments have not meaningfully addressed or solved despite its recognised community and economic impacts.

In many Australian jurisdictions, legislators (particularly elected representatives in local government) appear to be contemplating a form of inclusionary zoning. The Property Council's members are increasingly required to include affordable housing in their developments and

⁴ City of Melbourne Housing Needs Analysis, p 44

⁵ City of Melbourne Housing Needs Analysis, p 125

⁶ City of Melbourne Housing Needs Analysis, p 101

these policies have been created in an ad-hoc manner, often with no consideration of project-specific economic viability impacts which may result in the project not proceeding and exacerbating the lack of affordable housing.

Mandatory inclusionary zoning operates as a tax on at-market dwellings and can result in consequences that are counter to the policy objective of providing more affordable housing. Mandating affordable housing requirements in private developments poses a significant commercial disadvantage to landowners who purchased land at market prices based on prevailing policy settings, unencumbered by inclusionary zoning requirements. Mandatory inclusionary zoning effectively devalues sites currently held, commonly resulting in:

- sites not being sold or developed, limiting housing supply and further hampering the delivery of affordable housing and reducing affordability; or,
- additional costs being borne by other purchasers in the development through increased purchase prices in order to maintain project viability and secure finance.

Studies have shown that increased statutory “fees”, including costs associated with inclusionary zoning, can have significant negative effects on land prices⁷ and have found a significant negative correlation between those fees and the number of new homes built.⁸

Existing landowners should not be subject to changes in regulation which subsequently prevent or constrain their ability to develop or deal with that property. To do so fundamentally alters the premise upon which the land was purchased and amounts to a tax on that landowner. Changes in government policy to this effect create sovereign risk and discourage both individual and institutional investment in Victoria.

Notwithstanding the Property Council’s position on mandatory inclusionary zoning on private land, we acknowledge that there may be limited circumstances in which mandatory inclusionary zoning may be appropriate. This is the case where it:

- a. occurs on government land; and
- b. is clearly identified in any master planning or bid documents issued by government; and
- c. is not imposed after a procurement process.

Rather than the introduction of a tax to achieve affordable housing through mandatory inclusionary zoning, the Property Council instead recommends an approach whereby the private sector is appropriately and genuinely incentivised to provide affordable housing. Not only does this represent a fairer outcome for private landowners, it is more likely to provide greater amounts of affordable housing stock.

Earlier this year, the Property Council made a submission to the *Planning Mechanisms for Affordable Housing Ministerial Advisory Council*. Attached to this submission (**Attachment 1**) is the complete submission which outlines our full opposition to mandatory inclusionary zoning.

⁷ Ihlanfeldt and Shaugnessy, *An empirical investigation of the effects of impact fees on housing and land markets* (2004).

⁸ Skidmore and Peddle (1998).

While this submission was drafted before the COVID-19 outbreak, the 'sovereign' risk impacting investment in Victoria, along with the broader economic impact, has even greater emphasis now given COVID-19 than what was considered when the attached submission was finalised.

Develop affordable rental housing on City of Melbourne land

As stated above, the Property Council is supportive of the City of Melbourne and other municipalities delivering affordable housing on government owned land.

The City of Melbourne is proposing to deliver up to 25 per cent affordable rental housing on appropriate City of Melbourne land, with the leasing of land prioritised over the sale to retain public ownership.

The concept of leasing government land to help increase supply has merit, however, important consideration needs to be given to lease tenure to ensure viability for other uses (residential, office, retail) and to ensure investment and/or appropriate security is offered to be acceptable to the market.

The Property Council also supports investigations into affordable rental.

Strengthening internal affordable housing processes

The Strategy proposes developing an affordable housing planning policy for inclusion in the Melbourne Planning Scheme. We recommend that this policy clearly outlines examples of when an affordable housing contribution should be made, how the rate of affordable housing should be calculated and what should be included in an affordable housing agreement.

Prior to developing this policy, analysis is required to better understand and quantify the effects of affordable housing contributions upon proposed development to determine the appropriate and equitable rate of these contributions.

Section 3.2 proposes the establishment of a special purpose entity to manage affordable housing contributions, with the potential to operate across local government boundaries. While we are supportive of an approach that transcends local government borders, the Property Council believes this project best falls within the mandate of the State Government.

Under Section 3.3, the City of Melbourne would commit staff and budgetary resourcing to the ongoing delivery of affordable housing outcomes. The Property Council seeks clarity about how this would be funded, and assurances that this would not be supported through contribution funding.

Section 3.4 proposes developing a centralised internal process for recording and assessing affordable housing outcomes. The Property Council supports the recording and assessment of affordable housing outcomes; however, we believe consistency is vital to ensuring accurate statistics and understanding of need across Victoria. A state-based approach would more likely lead to greater affordable housing supply and prevent an inconsistent approach between councils. It would also better facilitate the delivery of affordable housing to targeted areas.

Advocate and partner for affordable housing

The City of Melbourne is proposing to lead and influence change across government, the community housing sector and development sector by doing and demonstrating best practice in its own operations.

The four proposed actions include:

- Advocating across all levels of government, the private sector and the broader community to improve affordable housing outcomes.
- Advocating to the State and Federal Governments for the increased investment and provision of social housing, with an emphasis on public housing.
- Partnering with the State and Federal Governments to identify surplus land for the delivery of affordable housing in the City of Melbourne. This may include land that is owned by government departments and entities such as Melbourne Water and Victrack.
- Using City of Melbourne events, public forums and media platforms to promote greater awareness and understanding of affordable housing issues and alternative housing models.

The Property Council is generally supportive of the proposed advocacy initiatives outlined above. It is critical that governments invest in the provision of social and affordable housing.

We support advocacy for increased government investment and appropriate frameworks to support industry action to deliver affordable housing. However, we are concerned that the model proposed by the City of Melbourne is too heavily reliant on “advocacy” to deliver much of the required stock.

According to the calculations provided in the Strategy, of the required affordable stock, the City of Melbourne would deliver just 1.5 per cent, the private sector would be responsible for 18.4 per cent, despite having finance and investor obligations, and advocacy would represent 65.2 per cent.

The practical application of this weighting means that if advocacy were unsuccessful in delivering dwellings, more than 53 per cent of the required stock would need to be delivered through an inclusionary zoning mechanism.

For the various reasons outlined above, it is not reasonable for the private sector to absorb such a high percentage of the burden. There has been chronic and repeated under-investment by successive State and Federal governments and forcing the private sector account for this lacuna is illogical and not sustainable.

With the economic impact of the coronavirus still unknown, it is not reasonable to place additional and disproportionate financial burdens on private sector businesses.

The Property Council has been a consistent proponent of the City Deal model and would welcome the opportunity to engage with the City of Melbourne to advocate in support of a deal for Melbourne.

Within Section 4, there is a proposal for affordable housing on commercial developments and community facilities on City of Melbourne land. We believe further consideration needs to be given to this point. We are also concerned that the strategy paper also mentions industrial land.

Positive incentives

The Property Council strongly supports investigations into supply-side measures to enable the delivery of diverse, secure housing stock, however this should not take the form of mandatory inclusionary zoning on private land. Priority should instead be placed on investigating new, secure housing assets such as build-to-rent. Incentives could include:

1. Relief from design standards – particularly size of apartments and shared communal areas.
2. Increased land release to increase supply.
3. Incentive payments or tax concessions for developers that include higher numbers of affordable housing dwellings.
4. Higher density / density bonus schemes.

Next steps

We look forward to continuing to engage with the City of Melbourne as it develops policies to support the delivery of affordable housing within the municipality.

If you require further information or clarification, please contact Emily Young, Senior Policy and Communications Advisor, on 0475 161 328 and eyoung@propertycouncil.com.au.

Yours sincerely



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