


JUNE 2021

The Rezoning 'Honeypot':

Evidence from Fishermans Bend



“The decision to rezone 250 hectares of inner urban industrial land to ‘Capital City Zone’ prior to undertaking the necessary strategic planning for such a major urban renewal task is unprecedented in the developed world in the 21st century ”

Fishermans Bend Ministerial Taskforce, 2015

Emily Sims & Jesse Hermans

Prosper Australia

emily.sims@prosper.org.au

@em_prosperous

@Prosper_Aust

Elements of this report are taken from a Minor Thesis by Emily Sims for the Masters of Urban Planning, University of Melbourne 2017. The authors would like to acknowledge the contribution and assistance of Prof. Carolyn Whitzman, Dr. Matthew Palm, Bryan Kavanagh, and Hamish Maggs. Technical appendices, including bases for valuation, are available upon request.

Executive Summary

Planning decisions that alter the nature or extent of property rights on land can generate large windfall gains on the value of that land. Rezoning windfalls have been described as a 'honeypot' for rent-seeking.

There is increasing awareness of the political-economic risk generated by the rezoning 'honeypot'; easy windfall gains create an incentive for landholders to lobby public officials, councillors and ministers for favourable rezoning decisions.

The circumstances surrounding the rezoning of Fishermans Bend, a 240-hectare brownfields precinct adjacent to the Melbourne CBD, provides for a simple quasi-experiment to quantify rezoning uplifts.

This study compares 2017 sales data for 33 properties in Fishermans Bend where there was a repeat sale at the time, to plot the rise in sale prices on a per square metre and per dwelling basis.

Results demonstrate large windfall gains to some properties when sold with planning permits in place. Planning permission was the clearest indicator of land uplift.

Overall, rezoning uplift was inconsistent. Uncertainty and politicisation of the planning process had negative impacts on the capitalisation of rezoning uplift.

Key findings include:

- + Rezoning uplifts did not consistently occur at FB until post-2015, due to uncertainty in the planning process.
- + For land without permits, the average is \$469 per square metre. The average uplift for permitted properties rises to \$1,726 per square metre. A planning permit therefore enabled an average return of 368% in our sample.
- + Based on these averages, total uplift estimated for 1,556 properties in the case study area (a portion of Fishermans bend) would be \$2.15bn without permits, or \$7.92bn with permits. The weighted average equates to \$4.43bn.

Such windfalls would likely cover the public investment needed for Fishermans Bend multiple times over, and is of a similar magnitude to Victoria's \$5.3bn social housing investment of 12,000 homes. This also equates to a whole year's worth of rezoning windfalls across the state, handed out overnight in a single rezoning.

Land value capture mechanisms, such as rezoning windfall gains taxation, could provide a source of infrastructure funds for urban renewal areas like Fishermans Bend and ameliorate the unproductive practice of speculative land flipping.

The Rezoning ‘Honeypot’

What are rezoning windfall gains?

The value of land is primarily determined by the net profit that can be generated at that location. The most profitable use of land is the ‘highest and best’ economic use. Property rights holders are able to claim a residual share of the income from their land, as rent or capital gains.

Land use planning regulates the way land is used and developed to provide broad environmental, social and economic benefits. Planning rules manage conflict, increase amenity; rationalise land use and coordinate public investment; generate synergistic exchanges; and enhance equity.

Regulatory limits in turn restrict the income generating potential of that land. Coordinating land uses across a region can conflict with maximising the value of any individual property. Hence, strategic planning creates winners and losers.¹

Planning decisions can generate large windfall gains on the value of land (also known as ‘betterment’). For example, when industrial land is rezoned to enable commercial or residential uses, the market value of that land often increases. This is because the expanded range or nature of activities permitted in that location increases profitability.

Another way to think about property is as a bundle of rights. When you purchase an industrial property, the bundle of rights includes the right to use the land for a factory or warehouse.² Rezoning changes the nature of those rights, adding new or more lucrative private property rights to the previously owned bundle. The value of the rezoning reflects what the market would pay if those new property rights were auctioned for sale.

¹Heritage and/or environmental protections act to suppress land values. Planning decisions can also cause ‘injurious affection,’ for example when a residential street is designated for arterial traffic. Governments also compulsorily acquire property for public purposes. These are sometimes described as ‘regulatory takings.’ There is a well established mechanism for compensating landowners for public acquisition, but no compensation for ‘downzonings’ such as heritage overlay. See Eccles, D & Bryant, T (2011) Statutory Planning in Victoria 4th ed. Sydney: The Federation Press.

²Furthermore, buying land in an industrially zoned precinct ensures that land uses around you are coordinated: you won’t get complaints about noise or noxious smells. Your use rights include that amenity.

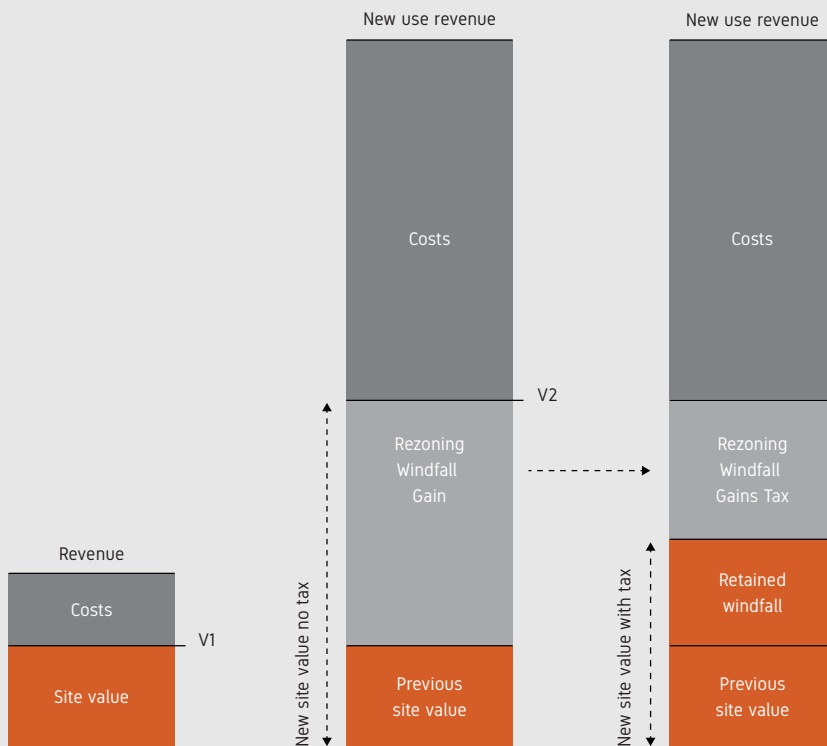


Figure 1: Site values under original and new zoning rights. (image source: Dr. Cameron Murray)

Figure 1 illustrates the change in value generated by rezoning. The differential between the market price of land prior to rezoning and the price after rezoning is a form of economic rent. This type of economic rent is easily generated in buoyant markets with high levels of demand. It has been described as a ‘honeypot’ for landowners seeking to capitalise on land use changes.

IN THE ABSENCE OF ANY MECHANISM TO DIVERT ECONOMIC RENT, REZONING CAN CONFER SUBSTANTIAL PRIVATE BENEFIT TO INDIVIDUAL LANDHOLDERS.

In Victoria, rezoning is initiated by the strategic planning process, either by state or local government planning authorities (councils) or the Minister for Planning. It involves making a formal amendment to a planning scheme.³ A Council will update their development controls to reflect new land-use needs and achieve policy outcomes. The Planning Minister can make amendments at their discretion. The powers are very broad, subject to only parliamentary oversight, making a Ministerial amendment the quickest and most cost-effective means to amend a planning scheme.

Third parties, often developers and/or landowners, can request rezoning (via a planning scheme amendment) be undertaken by a local council. These usually involve ‘spot rezoning’ of a particular locality or site. Proponent-led rezonings are extremely costly; subject to lengthy, expensive processes with uncertain outcomes. For these reasons we believe that proponent-led amendments are relatively rare. However, there is no readily available data on the frequency of proponent-led rezonings.

³ Victorian Department of Environment, Land, Water and Planning (2019) Using Victoria's Planning System https://www.planning.vic.gov.au/__data/assets/pdf_file/0017/95012/Using-Victorias-Planning-System-2015.pdf

Why do rezoning windfall gains matter?

There is increasing awareness of the political-economic risks generated by the rezoning ‘honeypot:’ easy windfall gains create an incentive for speculative land banking in strategic locations, as well as rent-seeking behaviour. This includes lobbying or corrupting bureaucrats, councillors and ministers to secure favourable rezoning decisions.

Investigative reporting into the rezoning at Fishermans Bend found well-connected insiders: “...party activists and donors who either bought into the renewal precinct before it was rezoned or were long-term property owners that pressed for redevelopment of the area.”⁴

The Victorian Independent Broad-Based Anti-Corruption Commission’s (IBAC) investigation Operation Sardon⁵ found numerous integrity issues involving planning and property development (in effect resulting from rezoning windfalls), such that it warranted an expanded scope of its ongoing investigation:

“THE INVESTIGATION HAS ALSO RAISED CONCERNS ABOUT THE RELATIONSHIP BETWEEN INDIVIDUALS INVOLVED IN PLANNING AND PROPERTY DEVELOPMENT IN OTHER PARTS OF VICTORIA, BEYOND CASEY, AS WELL AS THE WAY IN WHICH SUCH DECISIONS ARE MADE IN REGARD TO PLANNING AND PROPERTY DEVELOPMENT IN THIS STATE.”⁶

Similarly, NSW Independent Commission Against Corruption’s (ICAC) Operation Whitney is investigating allegations that a sitting MP improperly influenced local councillors to attain a favourable rezoning outcome for land his family owned.⁷

Well connected landowners in Queensland benefit from favourable rezoning decisions worth hundreds of millions of dollars, potentially billions over decades.⁸ Rent-seeking remains a risk so long as rezoning windfall gains can be captured by private landholders.

⁴ Millar, R, Vedelago, C & Schneiders, B. (November 1, 2015) Liberals profit at Fishermans Bend The Age <https://www.theage.com.au/national/victoria/liberals-profit-at-fishermans-bend-20151031-gknlaj.html>

⁵ <https://www.ibac.vic.gov.au/investigating-corruption/IBAC-examinations/operation-sardon>

⁶ IBAC (October 22, 2020) IBAC’s public hearings into allegations of serious corrupt conduct in relation to planning and property development decisions in Victoria to resume with expanded scope in November [press release] <https://www.ibac.vic.gov.au/media-releases/article/ibac-s-public-hearings-into-allegations-of-serious-corrupt-conduct-in-relation-to-planning-and-property-development-decisions-in-victoria-to-resume-with-expanded-scope-in-november>

⁷ ICAC (March 2021) NSW State Member for Drummoyne – allegations concerning improper influence and breach of public trust (Operation Whitney) [press release] <https://www.icac.nsw.gov.au/investigations/current-investigations/2021/nsw-state-member-for-drummoyne---operation-witney>

⁸ Murray, C. K., & Frijters, P. (2016) Clean money, dirty system: Connected landowners capture beneficial land rezoning. *Journal of Urban Economics*, 93, 99-114.

There is also recognition that a more equitable value sharing between the beneficiaries of rezonings and the public could reduce tax burdens elsewhere, and support investment in the public infrastructure required by intensified land use. Several recent reports highlight the importance of “value capture” as a form of beneficiary pays taxation.⁹

Value capture is described as economically efficient as public investments funded by land value uplifts can in turn support private sector development activity, feeding a virtuous cycle of urban development.

In Prosper’s 2019 submission to the NSW Review of Federal Financial Relations, we extrapolated revenue estimates from the ACT’s rezoning windfall gains tax – the Lease Variation Charge – to derive a broad estimate of revenue potential for other states. We estimated that a rezoning windfall gains tax could raise Victoria around \$5.7 billion per annum.¹⁰

For example, new transport access that reduces commuting times or opens up job-rich areas increases the value of land near stations. With more demand for housing and shops near stations, it makes sense to rezone for higher density uses. Intensified development entails further public investment in infrastructure and government services (such as parks and school teachers). Higher value activity on land, means higher land tax revenues, and around it goes.

In the absence of such schemes (and coordinated planning to ensure land is ‘set-aside’ for public infrastructure) the burden of taxation must fall on consolidated revenue.

IN THE CASE OF REZONING WINDFALLS, THIS CAN BE INTERPRETED AS A TRANSFER OF WEALTH FROM THE PUBLIC, WHO HAVING GIVEN AWAY EXTENDED PROPERTY RIGHTS, MUST THEN PAY LANDOWNERS FOR SITES OF STRATEGIC IMPORTANCE.

Controversy has accompanied land acquisitions at Leppington Square in NSW,¹¹ around the site of the new Sydney aerotropolis, as well as post-rezone acquisitions of school and park sites at Fishermans Bend.¹²

⁹ Infrastructure Australia (February 2016) Australian Infrastructure Plan Canberra: Infrastructure Australia. https://www.infrastructureaustralia.gov.au/sites/default/files/2019-06/Australian_Infrastructure_Plan.pdf; Infrastructure Victoria (2016) Value Capture: Options, Challenges and Opportunities for Victoria Melbourne: Infrastructure Victoria https://www.infrastructurevictoria.com.au/wp-content/uploads/2019/04/IV18-Value-Capture-Options_Final-web_v2_0.pdf; Prosper Australia (2019) The Transit Transformation Australia Needs https://www.prosper.org.au/wp-content/uploads/2019/09/Prosper_Hale_Transit_Transformation.pdf

¹⁰ Prosper Australia (21 November 2019) Submission to the Federal Financial Relations Review Panel https://www.treasury.nsw.gov.au/sites/default/files/2020-02/Prosper%20Australia%20submission%20to%20NSW%20Review%20of%20Federal%20Financial%20Relations_%2026%20Nov%202019.pdf

¹¹ Nguyen, K (25 May 2021) Report finds failures within government department over Western Sydney Airport land deal ABC News Online <https://www.abc.net.au/news/2021-05-25/leppington-triangle-report-into-western-sydney-airport-tabled/100162580>

¹² Millar, R & Lucas, C (October 20, 2015) Public pays for developer windfalls at Fishermans Bend, The Sydney Morning Herald <https://www.smh.com.au/national/public-pays-for-developer-windfalls-at-fishermans-bend-20151020-gkdydl.html>

Measuring rezoning windfalls at Fishermans Bend

Although rezoning windfalls are widely accepted as fact among planners, valuers and within the property industry, there are few studies which provide direct commentary.¹³

Quantitative research concerned with land-use regulation and land value uplift has usually asked whether zoning or urban containment has increased house prices.¹⁴ Looking at empirical evidence of rezonings can help us formulate policy that is cognisant of the way rezoning windfalls ‘play out’ in the market.

The circumstances surrounding the rezoning of Fishermans Bend, a 240-hectare brownfields precinct adjacent to the Melbourne CBD, provides for a simple quasi-experiment, using repeat sales data.

¹³ Geha, S.H. (2012) Measuring the interzonal price differential of land under varying land use controls (Doctoral dissertation) UNSW: Sydney. <http://handle.unsw.edu.au/1959.4/53423>

¹⁴ Recent studies in this vein include Kendall, R., & Tulip, P. (2018). The effect of zoning on housing prices. Reserve Bank of Australia Research Discussion Paper, (2018-03) <https://www.rba.gov.au/publications/rdp/2018/pdf/rdp2018-03.pdf> ; Greenaway-McGrevy, R., Pacheco, G., & Sorensen, K. (2021). The effect of upzoning on house prices and redevelopment premiums in Auckland, New Zealand. *Urban Studies*, 58(5), 959-976.; Murray, C., & Limb, M. (2020). We zoned for density and got higher house prices: Supply and price effects of upzoning over 20 years (No. zkt7v). Center for Open Science <https://econpapers.repec.org/paper/osfosfxxx/zkt7v.htm>



Figure 2: Artistic renders of Fishermans Bend Urban Renewal Area at allowable development envelopes under 2018 Fishermans Bend Framework. At the time of rezoning, allowable development was at densities similar to Melbourne's CBD pictured in the background. (Image source: Development Victoria)

The Fishermans Bend Rezoning

Fishermans Bend is situated at the mouth of the Yarra River. The area has a long history of heavy industry, including shipping and port activities, automotive manufacturing and aeronautics.

In February 2011, the Victorian Planning Minister announced that the area would become "Australia's first inner-city growth corridor", forecasted to support 80,000 residents at a density similar to that of Manhattan Island.¹⁵

On July 5, 2012, the precinct was rezoned from (primarily) Industrial 1 Zone (IN1Z) to Capital City Zone 1 (CCZ1) by ministerial decree.

Under Section 20(4) of Victoria's Planning and Environment Act 1987 (the Act) the Minister is not required to undertake the consultation normally required by a Planning Scheme Amendment, so the rezone took effect without warning.

At the time of the rezoning, Capital City Zone 1 had no effective density controls, poorly defined height controls, no effective controls influencing the setbacks between towers and off street frontages, and no requirements influencing internal dwelling amenity.

¹⁵ Johanson, S (February 18, 2011) 'Baillieu plans inner-city housing revolution' The Age <https://www.theage.com.au/national/victoria/baillieu-plans-inner-city-housing-revolution-20110217-1ay6t.html>

Since 2012, over 17,600 apartments have been submitted for planning approval within Fishermans Bend, most within high-rise towers. Figure 2 depicts existing and permitted development in neighbouring Southbank under the Capital City Zone.

The rezoned area is referred to as the Fishermans Bend Urban Renewal Area (FBURA) and consists of five precincts: Lorimer, Montague, Sandridge, Wirraway, and an Employment Precinct, now also designated as one of Melbourne's seven National Employment and Innovation Clusters.




Figure 3: Fishermans Bend Urban Renewal Area precincts and adjacent precincts (image source: Office of the Premier of Victoria)

The Minister set a flat rate Developer Contribution for Fishermans Bend, to be recovered through agreements under Section 173 of the Act. In 2013 the rate was \$15,900 per dwelling, \$180 per m² of commercial floor area, and \$150 per m² of retail floor area. These amounts were indexed to cover the future cost of building local infrastructure.

Ex-post strategic planning for FBURA introduced the strategic planning framework in 2014. This plan featured preferred height limits and 'light handed' strategic planning requirements.¹⁶ In 2015, the incoming government introduced enforceable height controls and effectively froze planning permit applications until a planning framework could be developed. At that time 26 permits had been issued, and a further 23 landowners submitted applications which were put on hold.

¹⁶ Fishermans Bend Advisory Committee (October 2015) Report 1 Fishermans Bend Advisory Committee. <https://vpa.vic.gov.au/wp-content/uploads/2014/07/FBAC-Report-Number-1-October-2015.pdf>



The subsequent strategic planning had to “work around” the density, heights and bulk those permits allowed. Once the Framework was adopted in 2018, the 23 properties with live applications had to go through a complex process with a review Panel to redesign their projects to fit within the revised planning framework.

The new Fishermans Bend Framework includes mandatory height limits and dwelling density ratios, as well as guidance on the location and staging of transport and community infrastructure.¹⁷

Planning at Fishermans Bend has been highly politicised. Public controversy has centred on extraordinary windfall gains to politically connected landholders. One prominent industry figure estimated land value uplifts of 500% due to the rezoning.¹⁸

¹⁷ Victoria Department of Environment, Land, Water and Planning (2018) Fishermans Bend Framework
https://www.fishermansbend.vic.gov.au/__data/assets/pdf_file/0020/35093/Fishermans-Bend-Framework.pdf

¹⁸ Millar, R. & Lucas, C. (October 20, 2015) Public pays for developer windfalls at FishermansBend Sydney Morning Herald
<http://www.smh.com.au/national/investigations/public-pays-for-developer-windfalls-atfishermans-Bend-20151020-gkdydl.html>

Study Methodology

This study is a relatively simple quasi-experiment, using observations on land values prior to zoning changes as the internal controls, and observations after the rezone as the treatment. The estimated land value is then adjusted to control for background land price inflation using data on industrial land values obtained from the Valuer-General.

Property developers use residual methods to determine the feasibility of redeveloping a site to highest and best use. The market value of the land is assessed in a redeveloped form using comparable sales data to find a gross development value at current market conditions. The cost of development is estimated and subtracted from the gross development value of the site. The change in residual land value of a parcel before and after the rezone is attributed to the change in the land-use regulation. Shane Geha quantified the land value uplift after rezoning in twenty cases in NSW using a residual methodology.¹⁹

Description of Sample

For this study, we looked at properties located within the FBURA that fell within the City of Port Phillip. Property data was sourced from VicMap Property Datasets, sales data was sourced from CoreLogic's RP Data portal and the Real Estate Institute of Victoria, as well as real estate industry news reports.

Of 1556 addresses in the case study area, 107 transacted after June 1, 2012. Of these, 43 properties had no relevant repeat sales history and were discarded. A further 21 properties were found to be strata titled. Due to the complexity of assembling strata titled parcels for development, and appraising their re-development value, these were omitted. Properties with sales earlier than 1989 were also omitted. This returned a sample of 33 freehold properties with relevant repeat sales.

Planning applications were scrutinised to determine date of effect and the intensity of proposal via the Urban Melbourne Project database (2017), the Department of Environment, Land, Water and Planning (DELWP) permit register, or the City of Port Phillip planning permit register. Proposed and permitted development yields were recorded to support land valuation at 'highest and best use'.

Valuation technique

Using desktop assessments of capital improvements, we estimated a site value at time of sale for each property transaction. A narrative detailing the basis of the valuation was recorded for each property.²⁰

Where relevant, capital improvements were valued at a depreciated replacement cost based on Cordell's commercial and industrial building cost guide.²¹ Where applicable professional fees i.e. architectural fees and due diligence, as well as demolition costs were estimated and land values adjusted on a residual basis.

Stamp duty and other statutory costs were not taken into account. Land was valued at highest and best use under the prevailing statutory regulations.

¹⁹ Geha, Measuring the interzonal price differential of land under varying land use controls Op. Cit.

²⁰ A technical appendix available upon request.

²¹ Cordell Commercial (January 2015) Victoria January 2015. Cordell Commercial and Industrial Building Cost Guide 38(1).

Land price inflation adjustment

To find the real sales price, we created a land price inflation index using ABS data on aggregated annual commercial land values in Victoria.²² Estimated site values were adjusted to find a real land value for the year of the subsequent sale.

How much would that same parcel cost if it were purchased in the year of the repeat sale, given underlying land price growth and inflation? For example 31-37 Buckhurst Street, South Melbourne was sold in 1985 for \$89,500, then again in 2014 for \$3.6m. What is \$89,500 worth in 2014 dollars given the “background” land price inflation?

To make the adjustment, the total land value for the year of the second observation was divided by total land values for the year of the first observation. This percentage change was then multiplied by the land value of the individual site at the first observation.

To estimate the value of the rezoning for each parcel, the adjusted before value is simply deducted from the post rezone value. Findings show the nominal value of the rezone at the date of the relevant observation. Where there are multiple sales before and after the rezone date, the adjustment is repeated to find the value of further planning interventions on the site i.e. issue of permits for use and development.²³

Desktop assessments are limited in several ways: in many instances, it was difficult to gauge the year of construction, or neighbourhood factors that may influence land values. In most cases capital improvements reflected obsolescent industrial stock. Under the Capital City Zone, these uses could not be considered highest and best use, and the sale price was taken to be land value.

As a reference point, a square metre average was derived from a small sample of comparable sales that could be confidently taken as land value. This average helped substantiate the value of Fishermans Bend industrial land for the years between 1991 and 2000. Nevertheless, all valuations have taken into account specific property attributes.

²² Australian Bureau of Statistics (2016) Australian system of National Accounts Table 61. Value of Land, by Land use by State/Territory time series spreadsheet cat. 5204.61 Retrieved 27/09/2017.

²³ The ABS land value data does not distinguish between commercial and industrial land-uses, and is aggregated at state level. This may obscure the difference in the value of allowable uses in industrial zones versus commercial zones and significant regional variation in land markets. Suspecting these factors introduced a downward bias, the results were tested against an adjustment index composed only of valuation data from industrial land in analogous municipalities. No significant variation was found.



Findings

Rezoning did increase land values in most cases where a permit was in place – in the majority of cases greater than \$1,000 per square metre, with the average rise being \$2,000 per square metre across large and small sites. Properties that did not have a planning permit achieved less land value uplift.

The distribution for land without permits was widely scattered with half the projects showing a negative impact of rezoning and an average of no change. This probably reflects buyer willingness to speculate on the likelihood of a permit being obtained – especially for smaller sites. These results demonstrate an uplift trend across a majority of the sample sites; however, the range is inconsistent.

Uplift in dollars per square metre

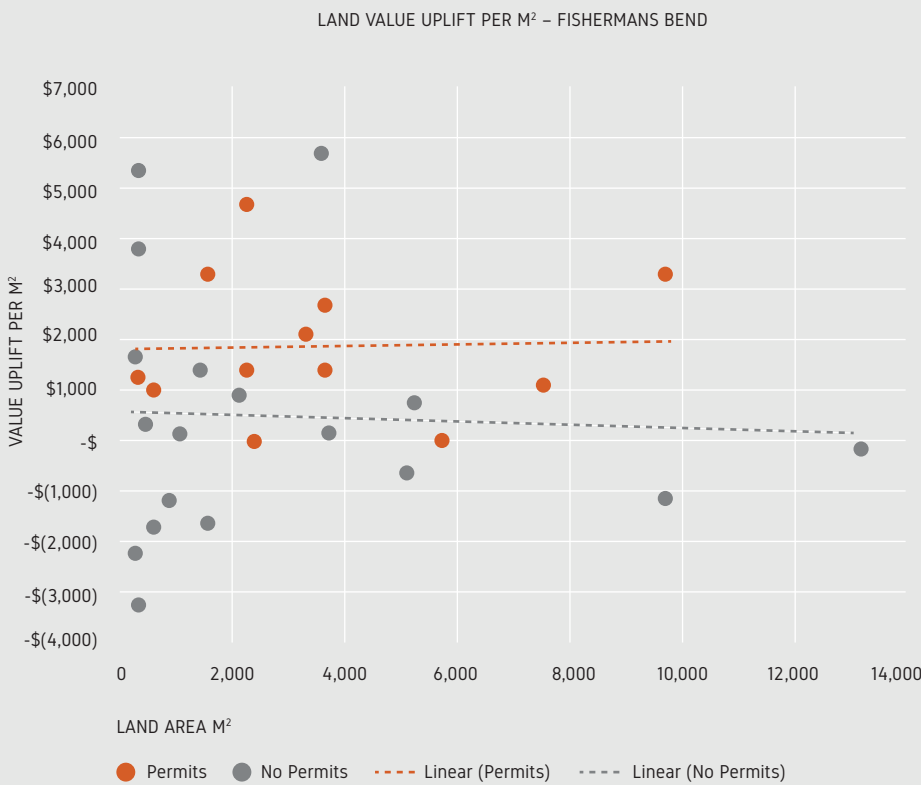


Figure 4 – Land value uplift per m²

When analysed on a per square metre basis, land size is an unreliable indicator of the value of rezoning uplift.

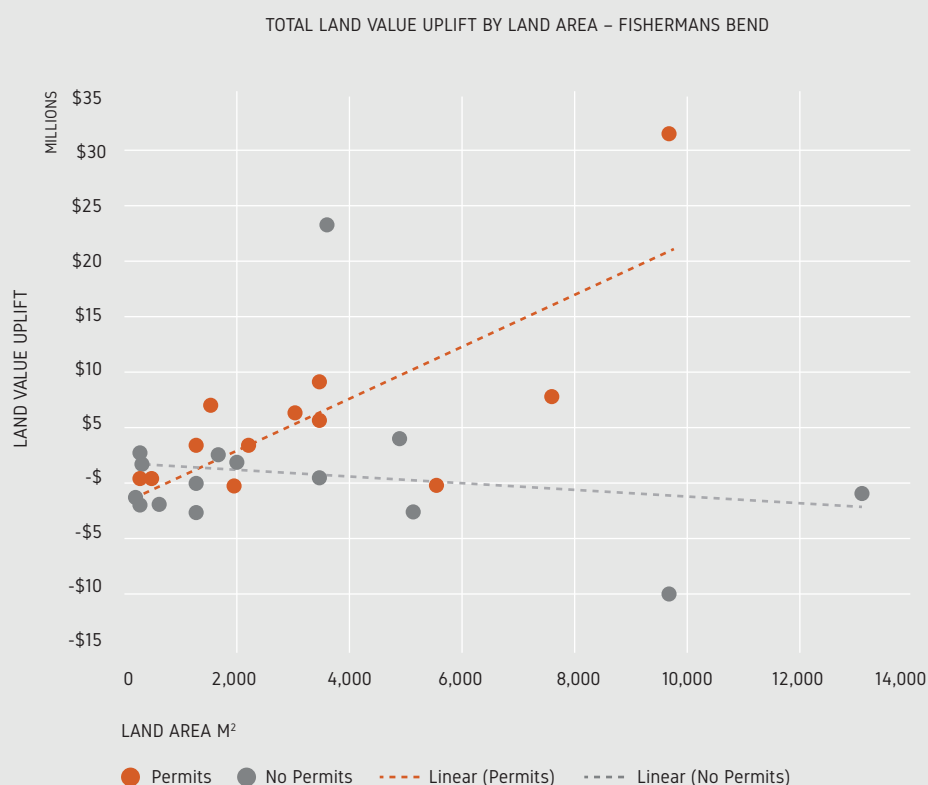


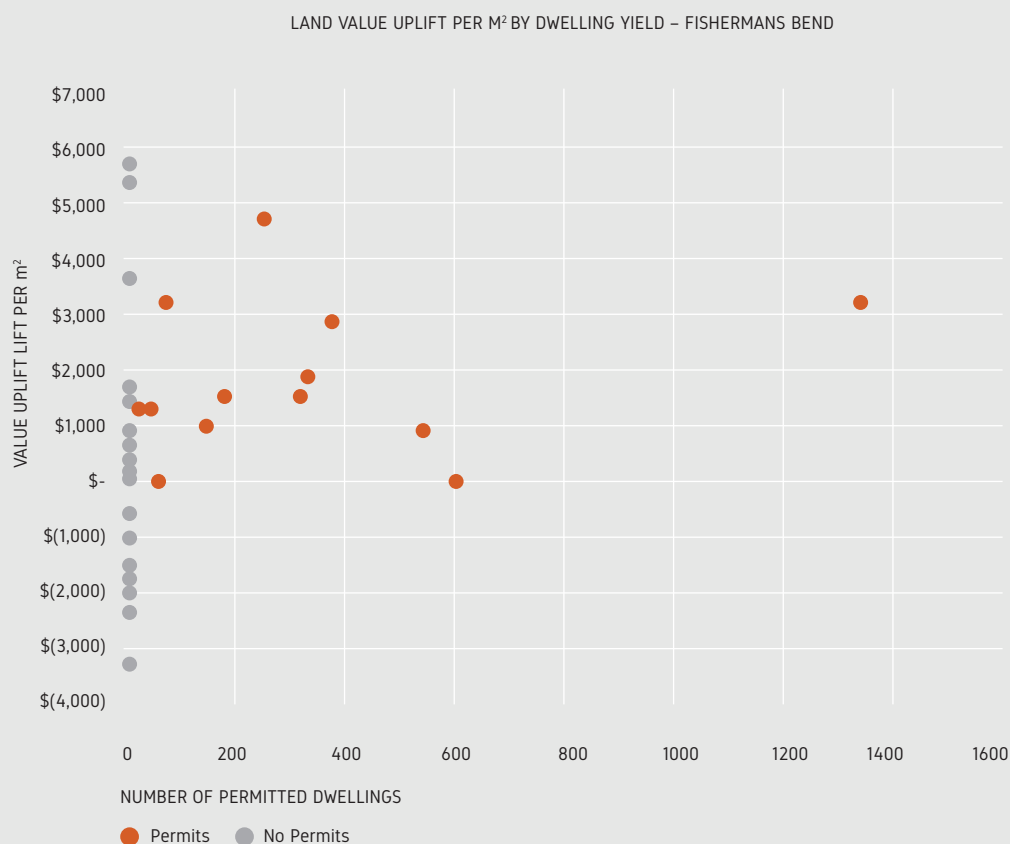
Figure 5 – Total land value uplift by land area

Uplift in total value

There is a clearer picture when looking at the total value of uplift. The sample yielded a high nominal uplift of \$31.7 million, and a low, negative uplift value of -\$10 million. The median nominal uplift is \$352 000. Larger sites obviously attract higher nominal uplifts. Uplift value increases as the site area increases. This is purely a function of the development envelope.

There is a weak but clear correlation between permitted development and increased returns to land. The average uplift for permitted properties rises to \$1,726 per square metre. For land without permits, the average is \$469 per square metre. A planning permit therefore enabled an average return of 368% in our sample.

In most cases, planning permission appears to be a crucial factor in the capitalization of the land rent into the price of property. Permitted development plans, and proposed plans, provide a high degree of certainty of the development envelope of a site. These findings support the claim made by the FBURA Ministerial Advisory Committee (2015), that without strong strategic planning in place, the statutory process becomes a means to ‘test’ the development envelope of a given site.



The intensity of development, as measured by the number of proposed dwellings, is also an unreliable indicator of expected uplift.

The results for small developments were very mixed but all larger developments obtained some value uplift. However, there was no relationship to the size of the development.

Dwelling yield was taken to be a proxy for the development envelope. Using dwelling yield as a proxy is an inferior measure to gross floor area. Unfortunately, gross floor area data was not readily available for each development proposal.

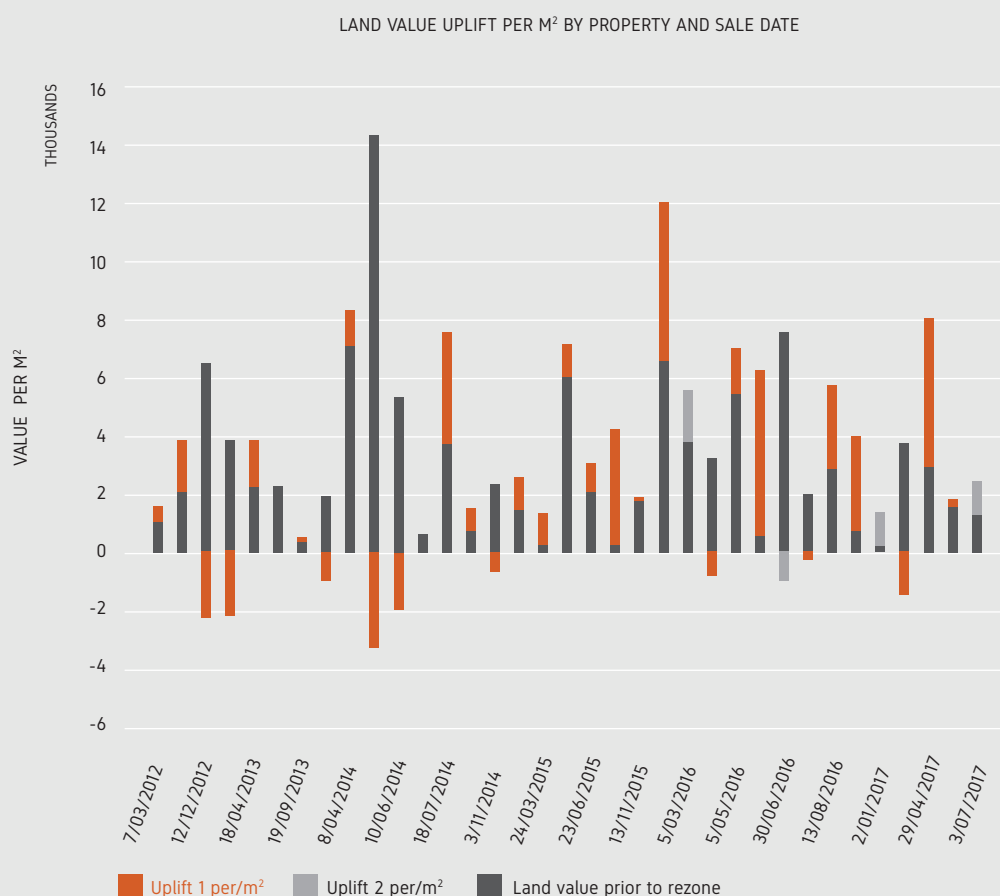


Figure 7 – Land value uplift per square metre by property and sale date

Timing of the sales

A further pattern emerges when the timing of sales is considered. Land value uplift was more consistent for properties sold after 2015 compared with properties sold immediately after the rezone.

There are several reasons why the timing of the sales may influence the value of rezoning uplifts:

- + A lack of demand in the market at that time. Low demand at Fishermans Bends was out of step with the wider Melbourne market; Melbourne's residential market grew strongly during this period.²⁴
- + Time lag may indicate a low supply of permit approved sites. Consider the timeline required to prepare a property for development (feasibility, design, due diligence, planning application, planning approval, marketing, and finally sale). A lack of "shovel ready" projects would suggest the market did not anticipate the rezoning.
- + Politicisation of the planning process. Later sales may reflect increased confidence after the change of government introduced a more robust planning process for FBURA.

²⁴ CoreLogic RP Data (November 2014) Quarterly Review: The Australian Residential Property Market and Economy Melbourne <https://www.corelogic.com.au/resources/pdf/reports/qtrly-economic-property-review--nov2014.pdf>

Negative rezoning uplift values

Of the 33 properties sampled, 7 returned a negative uplift value. This finding requires clarification: it does not mean that the property transacted at a loss. Our methodology uses a land price inflation index based on the aggregated annual commercial land values in Victoria. This approach attempts to capture the “background” growth in industrial land values at Fishermans Bend. In the 7 cases where there was a negative uplift, the sale price was lower than what we’d expect given state-wide commercial and industrial land price growth.

Property markets are complex and cyclical. There are many reasons why a parcel might trade for a lower price than expected. Firstly, there may be environmental or parcel specific factors that we simply could not see. This is a limitation of the ‘desktop’ valuation.

Another reason relates to the ‘redevelopment premium’ of the site. In their study of post-rezoning price uplift in Auckland, Greenaway-McGrevy et al. found that sites with recent capital improvements, enjoyed lower price appreciation after they were rezoned for higher uses.²⁵ Of the 7 negative uplift properties, 5 had valuable, income producing capital improvements that were less than 10 years old.

Potential impacts of contamination on land value

Properties with permits have greater information about extent and costs of remediation. The permit process triggers environmental auditing so sites with planning permits have undergone the Environmental Protection Authority’s audit process.

Fishermans Bend presents challenges in determining the extent of soil contamination to the cost of redevelopment. In 2012, Golders Associates estimated average remediation costs in Montague precinct of between \$3 million per hectare (ha) for medium risk sites and above \$6 million per ha for high risk sites. For sites with significant soil and/or groundwater contamination the estimate was up to \$10 million per ha.

A majority of parcels in the precinct held a medium degree of risk to development.

The case studies below offer a narrative illustration of the impact of rezoning on land values within Fishermans Bend.

²⁵ Greenaway-McGrevy, R., Pacheco, G., & Sorensen, K. (2021) Op. Cit.



Figure 8 – Citipower's Johnson Street substation (image source: Google Street View)

90-96 Johnson Street, South Melbourne – The \$22m substation

Figure 5 shows a particularly bold outlier in the “no permit” series that achieved a nominal uplift of over \$20 million (\$5,575 per square meter). This land value uplift is the highest in the sample, returning 11 times the \$469p/sqm average of non-permitted properties.

This property, 90-96 Johnson Street, is an exception because it has been an electricity substation since 1965. It is not a development site but is valued on “best and highest use”. The former State Electricity Commission sold the site in 1991 as part of the rationalisation of the Victorian electricity grid, relying on its then zoning to protect its future use.

This zoning was not protected when Minister Guy rezoned the whole area Capital City Zone. Yet, the substation played a critical role in power supply throughout the inner south east suburbs.

The private owner, a rather shrewd real estate agent, continued to lease the site to CitiPower. In the ten years prior to the rezone the annual rental had been around \$168,000 per annum. After 2012, the private landholder demanded much higher rent based on the appreciation in land values due to the rezone. The property was subsequently marketed as a development site with a significant holding income.

The operator, CitiPower, was forced to purchase the property in 2016 in order to secure permanent use of the site for electricity purposes. The price paid was excessive and ultimately passed on to electricity consumers.



Figure 9 – Approved development of residential apartments, townhouses and a hotel. Image source: urban.com.au

320 Plummer St. Port Melbourne – \$7 million windfall

320 Plummer Street, Port Melbourne is a 7,468m² site formerly used as the Rootes (Chrysler) factory. The property transacted in 2009 at a low price of \$230 per square meter.

Subsequent to rezoning, an application for a large mixed-use development was submitted to the Metropolitan Planning Authority (MPA) in 2014. The application proposed a large podium covering the entire site, with three residential towers located above.²⁶ A permit was granted in August 2015 by the Victorian Civil and Administrative Tribunal (VCAT).

Architectural renders in Figure 9 depict the permitted development of 443 dwellings including a mixture of apartments and townhouses, and 908m² of commercial floor area.

The property was subsequently purchased for over \$11 million by a local developer who substantially reworked the design proposal. An amended permit increased the yield to 547 dwellings including a residential hotel. Commercial floor space increased to 1305sq/m with the plans indicating a supermarket, and other retail. The property developer who eventually delivered the project was not the beneficiary of the rezoning uplift.

²⁶ City of Port Phillip (May 17, 2016) Agenda – Statutory Planning Committee – 17 May 2016. City of Port Phillip. Retrieved 11/10/2017.

Date of Sale	Use at Sale	Sale Price	Land value	Indexed value	Rezoning uplift
24/12/2009	Obsolete Warehouse	\$1,722,700	\$ 1,722,700	\$2,267,111	
24/03/2015	Vacant site with pending application for mixed use development	\$11,025,000		\$10,025,000	\$7,757,889

Land Area: 7,468 m². Source: RP Data, ABS

At the time of rezoning, FBURA was impacted by two relatively ineffective land value capture mechanisms: State land tax and a Developer Contributions scheme. Federal Capital Gains Taxation may have also applied, raising issues of vertical fiscal imbalance as the Federal Government does not directly contribute to the kind of infrastructure provision required at Fishermans Bend.


State Land Tax

To take the example of 320 Plummer St, Port Melbourne, based on an estimated land value \$2.27 million, land tax prior to rezoning was approximately \$42,975 per annum. After rezoning, based on a land value of \$10 million, land tax increased to \$182,475 per annum. The additional land tax represents only about 1.8% of the uplift in land value each year (or less than 8% over a 4-year holding period).

Developer contributions

Developer Contributions are not a price on the value of additional development rights. They reflect the additional costs of local infrastructure necessary to support the building – they are a cost of the building going ahead.

Developer Contributions only fund local infrastructure and do not contribute to state infrastructure – such as schools, parks and public transport. Over the last five years the Victorian government has spent over \$100 million on a new primary school, a park and two new tram stops to service Montague, with no return from the developments that have occurred.



Developer contributions are triggered later by building permits. Whoever constructs the project is required to pay 10% when building permits are issued, and the balance at the issue of title.

A purchaser will factor these expected costs into their total development cost when deciding how much to pay for the land. The cost is passed backwards to the land seller, or where market conditions allow, forward to the eventual buyer.

In 2013, the Developer Contribution for Fishermans Bend was \$15,900 per dwelling, \$180 per m2 of commercial floor area, and \$150 per m2 of retail floor area. For 320 Plummer Street, we estimate the developer contribution at \$7.2 million as a condition of the original planning permit, increasing to \$8.93 million for the higher yielding amended permission (plus indexation over 5 years).

We assume that the developer who purchased the site for \$11million was aware of their Developer Contributions liability and that they factored it into their residual.

THIS SUGGESTS THAT IN THE ABSENCE OF THE DEVELOPER CONTRIBUTION ENCUMBRANCE THE TOTAL VALUE OF THE ADDITIONAL PROPERTY RIGHTS WOULD HAVE BEEN CLOSER TO \$14MILLION. WITHOUT THE DEVELOPER CONTRIBUTIONS LEVY IN PLACE, THAT ENTIRE UPLIFT WOULD HAVE BEEN CAPTURED BY THE BENEFITTING LANDHOLDER.

Meanwhile, the revenue effort required to support development at Fishermans Bend would shift to other state taxes.



Figure 10 – 101 Salmon St, Port Melbourne permitted development (CHT Architects).
Source: urban.com.au

101 Salmon St Port Melbourne – Uplift only after permits

101 Salmon Street, Port Melbourne is a 3,287m² site in the Wirraway precinct. The site first transacted as unimproved industrial land in 2003. The property was not developed or subdivided, transacting again in 2013 within Capital City Zone 1. When the property was first sold after rezoning, the differential between the adjusted sale price and the rezoned sale price was found to be negative.

The location does not lend itself to residential development. There are few services in the area, no nearby shops and surrounding uses generate noise. It is serviced by bus but is not easily accessible.

Date of Sale	Use at Sale	Sale Price	Land value	Indexed value	Rezoning uplift
18/07/2003	Unimproved industrial land	\$2,655,000	\$2,655,500	\$6,399,231	
28/11/2013	Unimproved industrial land	\$3,492,500	\$3,492,500	\$4,414,601	(\$2,906,731)
7/3/2017	Permit granted 20/05/2015. Mixed-use development. 157 dwellings	\$8,580,000	\$8,080,000	\$8,080,000	\$3,665,399

Land Area: 3,287 m². Source: RP Data, ABS.

343 Williamstown Rd Port Melbourne – No zoning uplift at first sale

343 Williamstown Road is the site of an old, red brick workshop. This study found that the sale price of \$3m in 1999 was lower than the background inflation for industrial and commercial land. The value of the rezoning was not capitalised into the asking price by the seller.

Date of Sale	Use at Sale	Sale Price	Land value	Indexed value	Rezoning uplift
9/8/1999	Red brick single storey factory constructed circa 1970s – Depreciated value approx. \$400k	\$970,000	\$895,000	\$4,774,551	
4/6/2017	Unchanged from previous sale. Obsolete	\$3,000,000	\$3,000,000	\$3,000,000	(\$1,774,551)

Land Area: 1,278 m². Source: RP Data, ABS.

Rezoning windfalls capitalised into sites with planning permission

Only sites with permits consistently achieved rezoning uplifts above the background land price inflation. The pattern suggests that economic rents were capitalised into the land price after statutory planning permission rather than the initial rezoning alone.

Planning permits deliver certainty around the nature and extent of the property rights under the new zone (and the uncertainty of future changes of government policy).

Under the Victorian Planning and Environment Act 1987 a permit is a five-year guarantee that the State will enforce those property rights against claims made by the community, other property owners, or indeed the State itself. These permits are renewable.

In 2015, the incoming government completed the assessment of submitted applications resulting in twenty-six properties holding permits. Thirteen are represented in the present sample, having been sold after permits were issued. At the time of writing, two have been constructed and two others are currently under construction.

Although the approved permit holders were unaffected by the subsequent freeze on permit approvals, very few progressed with their projects. This was partly because the market for inner city apartments peaked in 2017 due to a series of policy changes in China and Australia regarding access to finance, resulting in large numbers of foreign buyers leaving the market.²⁷

Industry commentary pointed to the problems arising from an absence of coordinated planning: “Vague transport and infrastructure plans [at FBURA] specifically have undermined confidence. As a result, landowners have postponed construction and flipping approved development sites has become a common practice.”²⁸

A loss of confidence in the permanency of planning controls is a major factor to explain the absence of further rezoning uplift in FBURA (although these results may be biased downwards by forced sales and profit taking).

Another factor is the lack of certainty over the delivery of crucial government infrastructure such as the tram bridge to link Fishermans Bend to Docklands and the Melbourne CBD. This public investment would significantly improve access and hence further boost the value of sites along the proposed route.

Uplifts at Fishermans Bend did not happen “overnight”. Some properties demonstrated an immediate uplift in line with their (new) highest and best use. The purchasers acted with (potentially misplaced) confidence that these values would be realised. The tightening of planning controls at Fishermans Bend meant that developers in some cases paid more than the land is now worth.

There is debate among planners as to whether the level of discretion in the Victorian planning system contributes to poor outcomes on the ground. The system has been described as “high footprint, low impact.”²⁹ Woodcock et al. found that a significant number of developers ‘game’ the statutory system in order to increase density of their sites.³⁰ Permitted sites are then sold with a higher capitalised ground rent. Similarly, rezoning windfalls were tied up with successive expansions of the Urban Growth Boundary. The GAIC was partly designed to deal with this issue.³¹

Fishermans Bend is an abnormal case in the sense that markets could not speculatively ‘price in’ the rezoning windfall. Under a normal amendment process — one that involves advance notification and exhibition of draft planning changes, planning panel assessments etc. — we’d expect to see speculative capitalisation of rezoning windfalls. This is because a drawn out public conversation delivers a degree of certainty around the type, intensity and location of new land-uses before the rezoning is written into law. As discussed below, this has important implications for the design of rezoning windfall gains tax mechanisms.

²⁷ See for example: Wiltshire, T (Feb 21, 2019) Domain’s Property Price Forecasts – November 2018 <https://www.domain.com.au/research/domains-property-price-forecasts-801966/>

²⁸ Atkins, A (2016) “Melbourne’s hot spot for future apartment supply” Property Observer <https://www.propertyobserver.com.au/forward-planning/advice-and-hot-topics/50572-melbourne-s-hot-spot-for-future-apartment-supply-annabelle-atkins.html>

²⁹ Stephen Rowley, ‘Victorian Planning: Re-Thinking the Model,’ VPELA Revue, October 2019, 41–43.

³⁰ Woodcock, I., Dovey, K., Wollan, S., & Robertson, I. (2011). Speculation and resistance: constraints on compact city policy implementation in Melbourne. Urban Policy and Research, 29(4), 343–362.

³¹ Taylor, E. J. (2016). Urban Growth Boundaries and Betterment: Rent-Seeking by Landowners on Melbourne’s Expanding Urban Fringe. Growth and Change, 2(47), 259–275.0

Removing the honey pot

How can government's remove the 'rezoning honeypot'? Recommendations from governance experts have seen integrity measures adopted in several States, while economists suggest the use of revenue policy to remove the honey pot. This section provides an overview of the policy tools that have been proposed to address problems of speculation and public expenditure leakage in the rezoning process.

Integrity measures

Integrity and anti-corruption bodies do exist within all states, and these have coercive powers similar to Royal Commissions, with investigative, preventative, and educational functions. However, these can be undermined due to restrictions, or reductions in resources and jurisdiction.³² They are also limited in being able to address the honey pot issue, as discretionary rezonings and planning decisions are not inherently criminal acts - they are legal features of the planning system. In fact, Section 20(4) of Victoria's Planning and Environment Act 1987 legally empowers the planning minister to make unilateral decisions of State significance e.g. such as Fisherman's Bend, without notice or exhibition.

Developer donation bans or cooling off periods for politicians and bureaucrats can attempt to disrupt coordination to benefit from rezoning windfalls.³³ NSW has had a developer donation ban in place since 2009, with QLD adopting a similar ban in 2018. The ACT is set to enforce a donation ban from 1st of July 2021.³⁴

Other donations and electoral integrity reforms have been implemented, such as Victoria's 2017 electoral reforms.³⁵ These are significant, given the property and construction industry are some of the largest political donors.³⁶

However these measures do not fundamentally change the discretionary power of decision makers to afford favourable rezoning and planning decisions to the benefit of interest groups. Nor does it significantly hamper the potential favours that such interest groups can bestow upon decision makers.

³² Australian Senate Select Committee on a National Integrity Commission (2016), Interim report chapter 2: https://www.aph.gov.au/Parliamentary_Business/Committees/Senate/Establishment_of_a_National_Integrity_Commission/NIC/~media/Committees/integrity_ctte/Interim_Report/c02.pdf

³³ Murray, C. & Frijters, P. (June 2015) Four ways we can clean up corruption in land rezoning The Conversation <https://theconversation.com/four-ways-we-can-clean-up-corruption-in-land-rezoning-42557>

³⁴ ACT Government, Gordon Ramsay MLA Media Release (2020), Property developer donations to political parties banned in the ACT: https://www.cmtedd.act.gov.au/open_government/inform/act_government_media_releases/gordon-ramsay-mla-media-releases/2020/property-developer-donations-to-political-parties-banned-in-the-act

³⁵ Anderson, S. (28 Jul 2018), Victoria's got strict new laws on political donations but what does it mean? ABC News Online: <https://www.abc.net.au/news/2018-07-28/victorias-strict-rules-on-political-donations-explained/9997838>

³⁶ The Centre for Public Integrity (2021), Industry Political Donations and Disclosable Payments: Case Study: The property industry briefing paper: <https://publicintegrity.org.au/wp-content/uploads/2021/01/Donations-case-study-property-and-construction-industry-1.pdf>

There are still a number of longer term reciprocal favours within these networks that can be bestowed e.g. the revolving door - high paying positions in benefiting sectors (directors, lobbyists, advisors, consultants), in-kind gifts, publicity and media support for decisions etc. The situation is further complicated due to the nature of reciprocal favour trading, which is usually not direct and individualistic, but indirect and cooperatively tribal.

Another potentially effective means to address the honey pot is by vesting decision making in individuals or groups who cannot potentially benefit from bestowing favourable decisions e.g. (sortition) random outsiders from other jurisdictions with no prior local connections, citizens juries etc. with short tenures to prevent those connections from being developed. Several local governments already form citizens' juries to determine planning decisions.³⁷ This ensures that decision makers are more likely to favour the public interest, as there is minimal personal interest in favouring other interest groups.³⁸

Value capture

Mechanisms for capturing the uplift in land value due to public investment and community development fall under the rubric of "value capture."

The case for value capture is broader than addressing corruption in land use planning. It is made regularly by economists, planners, politicians, civil society, and government agencies - especially in contexts where land value uplift is demonstrably linked to community decisions and investments.³⁹ The rationale revolves around three broad aspirations:

- + **Deter corrosive speculation in property** – Windfall gains from rezoning invite corruption and nepotism in the planning process. Value capture could reduce undue private influence on policymakers by removing the incentive to rent-seek.
- + **Provide an efficient mechanism to fund infrastructure** – The marginal excess burden of land-based taxation is very low to negligible. As land is finite in supply and cannot be moved in response to taxation, value capture should not distort economic activity to the extent of other taxes, such as stamp duties. In the context of vertical fiscal imbalance, there is also a need to broaden the base of state taxation.
- + **Increase the horizontal equity of urban development** – In the absence of value capture, a few private beneficiaries enjoy all of any rezoning uplifts. Increasing urban density requires new and expanded infrastructure. At present, much of the funding for this infrastructure is drawn from general revenue and the burden falls on taxpayers who may not benefit from its provision. Value capture represents a fairer, 'beneficiary pays' model.

This report looks only at value capture mechanisms that can capture the uplift due to rezoning.

³⁷ Victorian Local Governance Association (n.d) Local Government Citizen Juries – Case Studies handout <https://www.vlga.org.au/sites/default/files/v4-Local-Government-Citizen-Juries-Case-Studies.pdf>

³⁸ Murray, C., & Frijters, P. (2017). Game of Mates: How favours bleed the nation. P. 76-78

³⁹ See for example Fensham, P. & Gleeson, B. (2003) Capturing Value for Urban Management: A New Agenda for Betterment Urban Policy and Research 21(1), 93-112.

Capital Gains Tax (CGT)

The Federal Capital Gains Tax is intended to partially capture capital gains, such as those private land holders receive from rezoning. However, the rate is low for land transactions (especially with the capital gains tax discount) and there is no mechanism for the Commonwealth to reinvest such gains into State infrastructure.

Developer Contributions

In Victoria, developer contributions are a critical source of finance for local government infrastructure. As the infrastructure they pay for (local roads, open space etc) are necessary for the sale of developed lots, they are essentially part of the cost of development – and directly tied to building approval rather than rezoning of the land itself. In Victoria, developer contributions are triggered by the issue of a building permit and settled at the issue of title, unless deferrals are enacted.

Rezoning Windfall Gains Tax (Betterment levies):

The charge for “betterment” (changes in land use) has existed across Australian states at different times.⁴⁰ As previously mentioned, the A.C.T. is an exception in having continuously charged for changes in land use since 1971. In the past, both Victoria and Tasmania have levied betterment levies at a rate of 50% of the uplift.

/ Growth Areas Infrastructure Contribution (GAIC)

The GAIC was intended to capture land value uplifts resulting from the expansion of Melbourne’s Urban Growth Boundary (UGB) in 2008. GAIC applies to “growth areas” on the peri-urban fringe, and is levied at a flat rate per hectare to all land over 0.41 hectares. GAIC payments are hypothecated to fund public transport and infrastructure such as schools and hospitals in growth area communities. Liability is triggered by subdivision, application for building permits, or land sale and has generous deferral provisions.

In theory, developer contributions and GAIC decrease the amount a developer can pay for the land, suppressing the residual land value. However, affected landowners did not adequately comprehend the basis of the tax, and strong political resistance resulted in major modifications. Land buyers were able to defer when GAIC was triggered, multiple times. Even then only 30% is payable and the rest can be paid in instalments. Consequently, the incidence of GAIC can be passed through to the final purchaser rather than the original landowner.

/ A.C.T. Lease Variation Charge

Value capture has been an integral feature of the Australian Capital Territory leasehold system since 1971. Under the ACT system, application to vary a lease for a new or more intensive use entails a one-off payment of 75% of the land value uplift. Where no uplift occurs, no fee is incurred.

⁴⁰ For example, NSW (Town and Country Planning Act 1945, later incorporated into the Local Government Act 1919, and the Land Development Contribution Act 1970 and Land Development Contribution Management Act 1970), Tasmania (Local Government Act 1962, ss.738, 739), Victoria Town and Country Planning Act, Section 196K, and Western Australia Town Planning and Development Act, Section 11(2).

This charge captures the value of the expanded development rights associated with planning permission.

THE LEASE VARIATION CHARGE HAS DEMONSTRATED CONSIDERABLE INSTITUTIONAL ROBUSTNESS, DESPITE NUMEROUS REVIEWS AND EIGHT REVISIONS. THERE HAS BEEN NO EVIDENCE THAT THE CHARGE DISCOURAGES DEVELOPMENT IN THE ACT.

/ NSW Land Development Contribution

In NSW councils were authorised to collect up to 80% of the uplift in 1945, however they did not make use of this power - supposedly due to failures in the valuation assessment design. The exception to this was the Land Development Contribution in the early 1970s, which corrected these issues.⁴¹ The levy was unique in that it did not go to consolidated revenue, but was hypothecated to pay for sewerage and other infrastructure costs associated with development of rural land (similar to the GAIC). It was levied at an arbitrary (and insufficient) rate of only 30%, and there were issues in how the levy was designed:

- + Difficulty in ensuring hypothecated funds were spent in a timely fashion on the needed infrastructure.
- + Vendors were allowed to stipulate in sales contracts that buyers would pay the levy (even if they didn't bear the true tax incidence), promoting the misconception the levy increased land prices.
- + The levy only captured value increases up until the moment land was rezoned, even though windfalls can take time to feed into the value of the next assessment.

This levy was abandoned after 3 years of operation, due to political pressure from landowners in a NSW by-election.

/ Development Rights Auction

São Paulo, Brazil utilises an innovative institutional framework for capturing rezoning windfall gains. Unlike betterment levies and other charges, this method highlights that windfall gains taxation isn't really taxation at all - it is the sale of additional development (or air) rights, little different to the sale of public land for private development.

The São Paulo model uses Certificates of Additional Construction Potential (CEPACs) - a form of charge issued by the city and sold in auctions in the stock market. Developers bid in a competitive market for the right to increase their development potential. What this amounts to is developers voluntarily choosing to pay a windfall gains tax, in turn highlighting that such charges for rezoning are not deterrents to investment.

⁴¹ Archer, R. W. (1976). The Sydney Betterment Levy, 1969-1973: an experiment in functional funding for metropolitan development. *Urban Studies*, 13(3), 339-342.



Tax incidence

Who pays when we tax rezoning windfalls?

Tax incidence (who pays) can be distinguished into legal incidence (who transfers funds to the government), and economic incidence (who is made worse off by the tax). Normally people conflate both legal and economic incidence, assuming the one who pays tax is the one who is worse off. However this is not always the case. The incidence of a tax depends on whether taxes can be passed on, absorbed, or passed back through the market.

Unlike GST, which taxes production of goods and services and is thus passed on to buyers to maintain profitable production, taxes on land (including rezoning windfall gains taxes) are passed back onto the holders of land. This is because the supply of land is fixed, and so its value is purely determined by what buyers are willing or able to pay.

TAXES ON LAND DO NOT INCREASE A BUYER'S WILLINGNESS TO PAY FOR LAND
- THEY REDUCE IT, IN TURN FORCING LANDHOLDERS TO SELL THEIR LAND FOR
LESS AND ABSORB THE ADDITIONAL TAXES.

Landholders cannot reduce the supply (or “stop production”) of land. The only way to avoid such taxes is to sell their land to others.

Developers cannot reduce their tax burden by refusing to develop, and so the incentive and feasibility of development is not undermined by such taxes. Land acquisition subject to a rezoning windfall gains tax will be factored in by developers into their feasibility and willingness to pay (for the residual land value), and so land acquisition costs will not change for developers.

The ACT experience demonstrates little pass through of its lease variation charge to homebuyers. A recent 2019 review⁴² and consultation⁴³ reaffirmed the findings of the 2012 ACT Tax Review:

“THERE IS NO SUBSTANTIVE EVIDENCE (EVEN WHEN INDUSTRY IS CHALLENGED TO PRESENT IT) TO DEMONSTRATE THAT TAXING REZONING UPLIFTS IS PASSED ON INTO HIGHER PRICES. INDEED ONLY PROPERTY GROUPS APPEAR TO OPPOSE THE CHARGE, WHEREAS COMMUNITY GROUPS SUPPORTED IT - INDICATING WHICH GROUP REALLY PAYS.”⁴⁴

This also aligns with evidence from São Paulo, where developers must bid for the full market value of additional development rights. If developers were refunded what they paid, would they pass on these savings in lower prices?

JUST AS SELLING PUBLIC LAND AT MARKET VALUE DOES NOT MAKE DEVELOPMENT UNPROFITABLE OR INCREASE MARKET HOUSING COSTS, NEITHER DOES CHARGING A PORTION OF THE MARKET VALUE FOR A REZONING WINDFALL GAIN.

Who pays when we don't tax rezoning windfalls?

The real issue with failing to tax rezoning windfalls is who pays if landholders do not. If governments give expanded property rights to landholders gratis, then other taxpayers must foot the bill for the infrastructure required to serve more intense land uses. These taxes usually fall on productive business activities e.g. payroll tax (a literal tax on jobs and wages), which in turn reduce prosperity.

If taxes are not increased, we must simply make do with less: less infrastructure, fewer public services, and lower quality of life in growing communities. In either case, the wellbeing of the broader community suffers if we fail to tax rezoning windfalls.

Tax design considerations

In practice, the challenge for taxing rezoning windfall gains are in getting the design and implementation right. At best, a rezoning windfall gains tax is highly efficient with no economic distortions, and has a modest administration cost. At worst, poor design can result in high administration costs, with minimal windfall gains recovered.

There are also possible equity issues to consider in the transition. For sites where rezoning was imminent and inevitable, rezoning windfalls have usually capitalised into market prices. Some developers may have bought sites for development at over-inflated “already rezoned” prices. In these cases, where market expectations have formed around a rezoning windfall, the previous vendor is likely to have captured much of the uplift. In these cases, a developer may be forced to on-sell the site, rework projects feasibility, or renegotiate options contracts to account for the changed tax environment. This may slow the pace of development in the short-term.

⁴² Consultation paper, Review of the Lease Variation Charge Sept 2018: https://s3.ap-southeast-2.amazonaws.com/hdp.au.prod.app.act-yoursay/files/6215/3688/6997/Lease_Variation_Charge_consultation_paper_PDF.pdf

⁴³ Detailed Consultation Report, Review Of The Lease Variation Charge Feb 2019: https://s3.ap-southeast-2.amazonaws.com/hdp.au.prod.app.act-yoursay/files/8615/5132/8561/Detailed_Consultation_Report.pdf

⁴⁴ ACT Taxation Review May 2012, p. 99-100: <http://www.treasury.act.gov.au/documents/ACT%20Taxation%20Review/ACT%20Taxation%20Review%20May%202012.pdf>

BUYING A SITE PRIOR TO REZONING AT “ALREADY REZONED PRICES” IS STILL A SPECULATIVE RISK, AND ONE THAT BUYERS VOLUNTARILY TAKE ON. DEVELOPERS ARE ALWAYS FREE TO BUY AND DEVELOP SITES THAT ARE ALREADY REZONED.

These issues also come down to when the before and after valuations for determining the windfall gains are made. This is in turn affected by what trigger is used to determine when the tax liability is to be paid, and who is obligated to pay the tax to the government. Ensuring these details are correct is crucial to ensure the honey pot is removed.⁴⁵

	Valuation Assessed	Basis of Assessment	Legal Incidence	Liability Deferral Period	Payment Due	Indexation Rate
Scenario 1	Gazettal date of planning scheme amendment	Valuer General annual assessments	Title holder on date of gazettal	No Limits to deferral	At point of liquidity e.g. sale or subdivision	Aggregate land price inflation
Scenario 2	Issue of permitted for use or development	Residual of permitted development	Permit applicant	Limited deferral period e.g. 4 years	At point of liquidity e.g. issue of certificate of occupancy	Aggregate land price inflation

The table above considers two tax design scenarios:

Scenario 1

In scenario 1, the value of the rezoning windfall is based on the assessed value of the land before and after the rezoning date - when the planning scheme amendment is published in the government gazette. The valuer-general is required to assess value annually for state land tax and council rates.

In this scenario, a notice of assessment is issued to the property holder, as with council rates.

The property holder should then be given the option to defer the tax until a point of liquidity such as sale. At this point, the rezoning tax is payable.

Where the nominal and economic incidence falls on the seller it is reasonable to allow deferral indefinitely to avoid the perverse effect of forced sales or land-use change. The liability must be indexed, ideally to some measure of aggregate land price inflation. It is crucial that the liability keeps pace with land price inflation. If not, the liability will shrink as a proportion of the real value of the rezoning - increasing the profitability of deferring development and holding on to sites for higher prices.

The key benefit of this approach is that the legal incidence of the tax travels with the

⁴⁵ Murray, C. (May 31, 2021). Explainer: Taxing rezoning windfalls (betterment). Henry Halloran Trust- University of Sydney. <https://doi.org/10.31219/osf.io/n78m4>

beneficiary of the rezoning - the landholder. If the seller is liable to pay, the sales price on the market is the same, and the tax comes from the vendor.

Piggybacking on the existing valuation for land tax purposes makes the administration of the new tax relatively straightforward. However, statutory valuation assessments are necessarily conservative. It is difficult to assess what the final use and/or development could be in a highly discretionary zone. In the Fishermans Bend sample, permits were the clearest corollary of rezoning uplift value. Also, several properties achieved multiple uplifts as previously issued permits were amended and expanded.

Like other property taxes such as stamp duties and land taxes, a rezoning windfalls tax encumbrance on a land title will reduce its value (relative to no tax). The market sales value of a title will be dependent on who is liable to pay. So, a worse outcome would be a situation where the assessable value is at the date of gazettal, but the buyer is liable for the rezoning tax. The tax then becomes embedded in an equivalent lower sale price. This issue is relevant for determining pre and post rezoning values, as post-rezoning values will be artificially lower if the buyer is liable to pay the tax.⁴⁶

Another issue arises if the comparable sales used to benchmark statutory valuations are speculative. Property markets often speculatively price the value of rezoning or infrastructure into sales well prior to delivery or formalisation.⁴⁷ Rezoning windfalls will capitalise after the announcement of a rezone.⁴⁸

If local comparable sales are used, the rezoning windfall may be underestimated. An alternative to comparable sales to determine land value would be comparable existing use rental income values and a benchmark capitalisation rate. Conservative valuations of the post-rezoned value will also reduce the potential estimates of windfall gains. However, this raises the issue of transition fairness, as discussed above.

Scenario 2

In scenario 2, the value of the rezoning windfall is based on the value of permitted use and/or development under the new zone. The two benchmark values are the current value assuming the current use is the highest and best use, and the value of the new, approved use.

In this scenario, the permit applicant is liable for the tax, as for developer contributions. Payable at the point of liquidity - sale, issue of certificate of occupancy.

Permit amendments allow for additional taxes to be paid on any additional uplift. This makes keeping track of multiple zoning changes and sales unnecessary (including where final permitted development exceeds discretionary limits). It also simplifies valuation and comparison of sales data, as properties are not encumbered with past tax liabilities. The only necessary record is past taxes paid (to ensure no double taxation).

⁴⁶ The market price with a betterment tax in this scenario will be the pre-rezoning price plus the full betterment divided by one plus the tax rate (after rezoning price = before rezoning price + total betterment / [1 + tax rate]).

⁴⁷ See, for example, Yen, Barbara T.H. & Mulley, Corinne & Shearer, Heather & Burke, Matthew, (2018) "Announcement, construction or delivery: When does value uplift occur for residential properties? Evidence from the Gold Coast Light Rail system in Australia," Land Use Policy 73(C): 412-422.

⁴⁸ Incidentally, this was one of former Planning Minister Matthew Guy's primary rationales for rezoning Fishermans Bend without prior notice. To avoid speculative 'run up'.



As the nominal incidence of the GAIC falls on the land buyer (often the developer) extended deferrals may challenge the incidence of the tax. Deferrals are cited anecdotally as a problem with the design of Victoria's GAIC. The longer the delay, the longer a vendor can bank a site until the land price inflation exceeds the GAIC liability. With less market competition at the price per square metre at the time of rezoning, the developer may hold out for higher prices to cover the cost of tax.

The ACT system prevents landbaking by limiting deferral to a four year period. This seems appropriate where rezoning liability coincides with development approval.

We recommend an indexation at an appropriate land price inflation rate.



Conclusion

The rezoning of Fishermans Bend was unprecedented. Ultimately, the government responsible was punished at the ballot box. However, it would be wrong to assume that a case like Fishermans Bend could never happen again. The eye-watering powers of the Planning Minister to rezone without public notice remain. The 'rezoning honeypot' remains available to beneficiary landowners; an incentive for rent-seeking. Land prices are rising rapidly, and industry continues to complain of constrained developable land supply. The economic and legal conditions that led to the Fishermans Bend rezoning have not changed, though there is now greater public awareness of the risks.

Rezoning windfall gains are publicly created value, and currently form a private honey pot that is prone to corruption. We can readily recover this value to remove the honey pot, providing an efficient, equitable, and sustainable revenue stream - sharing rezoning windfalls with everyone, and not just a few well connected insiders. We endorse moves to tax rezoning windfall gains in Victoria, and urge that these taxes be expanded, and adopted in other states. This will ensure that another Fishermans Bend never happens again, saving taxpayers and the public from footing the bill.

Prosper Australia
Level 1, 64 Harcourt Street, North Melbourne 3051
prosper.org.au

