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Funding and financing faster rail

Overview

2.1 This report builds on the House of Representatives Standing Committee on Infrastructure, Transport and Cities' (the committee) work in the previous parliament. In its earlier reports entitled *Harnessing Value, Delivery Infrastructure* and *Building Up & Moving Out* the previous committee recognised the importance of:

- master planning to drive the development of Australia's major cities and regional areas
- the economic, social and community benefits of transport connectivity between major cities and regional areas
- investment in major infrastructure, including rail projects, as an economic driver
- all levels of government collaborating to explore innovating financing and funding approaches for delivering infrastructure projects
- considering and utilising value capture to reduce the burden on taxpayers.

2.2 In this report the committee focuses on exploring opportunities for using value capture for funding rail infrastructure projects.

2.3 The committee is pleased to see the trend in recent years of Australian Government, and state, territory and local governments, increasingly exploring and applying innovative financing and funding approaches to rail and other infrastructure projects.

2.4 This chapter firstly sets the scene with key themes and mentions a selection of innovative approaches to financing and funding rail projects. While acknowledging the distinctions between financing (upfront payments to build the infrastructure) and funding (paying for the infrastructure over its lifecycle), discussion of these approaches are not compartmentalised, and occur throughout the relevant sections.

2.5 Secondly, the committee recognises that the Australian Government will continue to play the key role in funding and providing strategic leadership on infrastructure projects. The section on the role for government highlights the need for the Australian Government to provide leadership, and work with state, territory and local governments, particularly in the areas of land planning, protecting rail corridors, and maximising opportunities for value sharing where government rail projects create significant property value uplift for private beneficiaries.

2.6 Thirdly, what was also clear during this inquiry is that there is still more work to be done on incorporating direct value capture and value sharing mechanisms into infrastructure projects.

2.7 In the context of value sharing and value capture mechanisms, these sections explore: opportunities in the vicinity of rail stations and precincts; what constitutes a 'just, equitable and fair' portion for value sharing; and a selection of value capture mechanisms.

2.8 In the sections on value sharing considerations and limitations, the committee discusses value escape in the form of opportunities missed where private beneficiaries have enjoyed significant property value increases due to infrastructure projects, wholly, or partially, funded by the Australian Government. It also covers value capture limitations, and why it is important for the Australian Government to act promptly on land planning, corridor preservation, and locking in base land values in areas identified for future rail projects.

Key themes

2.9 *Financing* infrastructure projects involves paying for the upfront costs of building the infrastructure asset, such as the rail line. The main options for financing infrastructure projects are: public procurement (the government finances and owns the asset) and private investment (the private sector finances and owns the asset). Public–private partnerships (PPP) represent a combination of these approaches. Broadly, financing for infrastructure projects can be done through:

- public financing—from general budget appropriations for infrastructure projects (through tax revenue or government debt, revenue bonds tied to specific infrastructure projects, or infrastructure investment by government trading enterprises[1])
- private financing—from private investors (such as banks, pension funds, insurers and private equity firms) for specific projects.[2]

2.10 *Funding* infrastructure is how the project will be paid for over its lifecycle. Essentially, there are two sources of funding for infrastructure projects: tax payers and beneficiaries (user charges). In addition, governments can seek to create and capture value generated from infrastructure projects.

2.11 Value creation and value capture opportunities for infrastructure projects were discussed in detail in the previous committee's reports entitled *Harnessing Value, Delivery Infrastructure* and *Building Up & Moving Out*.

2.12 Value creation involves creating greater public value beyond the immediate focus of the project, by considering wider opportunities that are available. This can include economic, social and environmental benefits.[3] In the *Harnessing Value, Delivering Infrastructure* report, the previous committee concluded that 'value creation is one of the key purposes and outcomes…of improved transport connectivity', and that the creation of value, and its capture, provide the means to pay for the enhanced connectivity.[4]

2.13 Value capture is a means by which governments can fund part, or all, of the costs of infrastructure projects, and in time achieve profitable outcomes. In the context of rail infrastructure projects, value capture mechanisms can be used to capture uplift in value generated by new rail infrastructure, such as increases in property values in proximity to rail stations and along the rail corridor. Through taxation or other mechanisms, governments can capture a proportion of that value uplift

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1 Government trading enterprises are also known as public trading enterprises, government business enterprises, public corporations, state-owned enterprises or government corporations. Australian examples in the communications sector at the Australian Government level are the NBN Co and Australian Post, and in the transport sector at the state level, the Public Transport Authority (Western Australia) and Sydney Trains (New South Wales).

2 Chong S and Poole E, *Financing Infrastructure: A spectrum of country approaches*, Reserve Bank of Australia Bulletin, September Quarter 2013, pp. 66-68.

3 Victorian Government, *Value creation and capture framework*, p. 9, <https://www.vic.gov.au/value-creation-and-capture-framework>, accessed 5 November 2020.

4 House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Harnessing Value*, *Delivering Infrastructure*, November 2016, p. 104.

that can be used to help fund that specific project and/or other infrastructure projects.

2.14 When used in this report, 'value escape' refers to public spending on infrastructure that directly leads to private benefits that are not directly captured and shared by government. In this context, a clear example of this is the increase in property values near a rail development, which result from infrastructure wholly, or partially, funded by the Australian Government. Without a system for 'value sharing'/value capture in place, governments, and taxpayers, miss out on their share in a portion of these property value increases, which instead go to speculators or landowners.

2.15 The committee recognises that value capture is only one part of the bigger financing and funding picture when it comes to major infrastructure investment, including rail projects, and that there are a complex range of factors that can contribute to increases in land values.[5] When seeking a fair and equitable return on government infrastructure investment, it would need to be clear that the infrastructure investment itself, combined with rezoning, was the sole or primary cause of the property value uplift.

Innovative approaches by government

2.16 Governments will continue to play a key role in funding infrastructure and guiding financing approaches. In recent years, governments have changed the way they consider and structure infrastructure spending.

2.17 From 2019-20, the Australian Government will invest over $13 billion through innovative financing options, such as concessional loans and equity injections. Rather than simply providing funding for new projects, the Australian Government has recognised the value of being an 'active, informed investor'.[6]

2.18 When considering innovating financing and funding options, the Department of Infrastructure, Transport, Regional Development and Communications website lists a range of mechanisms, including:

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5 Mr Barry Broe, CEO, National Faster Rail Agency (NFRA), *Committee Hansard*, 23 June 2020, Canberra, p. 4.

6 Department of Infrastructure, Transport, Regional Development and Communications, *Innovative funding and financing*, <https://investment.infrastructure.gov.au/about/funding_and_finance/index.aspx#about>, accessed 6 November 2020.

concessional loans; guarantees; phased grants and available payments; equity injections; value capture; and wider use of user charging.[7]

2.19 In its *Principles for Innovative Financing*, the Australian Government recognised that delivering critical transport infrastructure will require:

- active partnerships with state and local governments and the private sector
- re-evaluating how transport is funded and how financing is structured
- improving the long-term sustainability of land transport funding by looking beyond traditional approaches to infrastructure funding.[8]

2.20 In their joint submission, the Infrastructure and Project Financing Agency (IPFA) and National Faster Rail Agency (NFRA) argued that to achieve the objectives in the *Faster Rail Plan*, alternative financing options will need to be pursued, including:

- conditional grants— provided by the Australian Government, state or local governments to assist the funding of large infrastructure projects such as faster rail projects
- debts (loans)—the Australian Government borrowing at a lower cost and over a longer period than possible for the other tiers of government or private sector, which can then facilitate Australian Government concessional or non-concessional loans for rail projects
- equity—contributing capital to acquire a direct interest in a project, with an expectation of future returns from project profits and distributions
- guarantees—by the Australian Government, state or territory governments to support repayment obligations for project debt.[9]

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7 Department of Infrastructure, Transport, Regional Development and Communications, *Innovative funding and financing*, <https://investment.infrastructure.gov.au/about/funding_and_finance/index.aspx#about>, accessed 6 November 2020.

8 Department of Infrastructure and Regional Development, *Principles for Innovative Financing*, <https://investment.infrastructure.gov.au/about/funding_and_finance/principles_for_innovative_financing.aspx>, accessed 3 November 2020.

9 Infrastructure and Project Financing Agency (IPFA) and NFRA, *Submission 8*, pp. 15-17.

2.21 IPFA and the NFRA also submitted that, with tight constraints on grant funding, value capture and farebox revenue need to be considered:

- Value capture, which includes:
  - ⇒ passive value capture—where government secures increased revenues from an infrastructure project without taking any further action. For example, where rail projects drive increases in property values along the rail corridor or near stations, this will increase federal and state government revenues from income tax, stamp duty and capital gains tax.
  - ⇒ active value capture—where it is planned that additional revenue will be generated from the main project. For example, if a new faster rail line is built by the government or a company, and it also owns property in the corridor it can directly benefit from increased property values. Alternatively, a state government can sell development rights around a new rail station or implement a new tax or levy linked to the precinct.
- Farebox recovery—generating revenue from rail users, generally through ticket sales.[10]

2.22 In its submission, the Property Council of Australia identified a range of options for funding infrastructure projects, including:

- government grant funding—infrastructure investments funded from general taxation, sometimes supplemented through user charges, as the benefits are directly or indirectly shared across beneficiaries
- asset recycling—the leasing or sale, in whole or part, of infrastructure which can be more effectively operated and managed by the private sector, where proceeds are reinvested into infrastructure
- user charges—the creation of a revenue stream funded by the direct users over the lifecycle of the infrastructure
- network wide farebox surcharges—users of the broader network benefit from major system upgrades due to infrastructure investment
- betterment tax levy—captures a portion of the estimated value uplift on land (residential, commercial or both) within an infrastructure catchment area, calculated on above market increases in land values, levied annually

10 IPFA and NFRA, *Submission 8*, pp. 18-20.

- rate surcharge on residential property/businesses—a surcharge on residential property/businesses set at a low rate would provide a revenue stream to borrow against to contribute to funding infrastructure
- intensifying development around new infrastructure—where the Australian Government places stronger conditions on funding, or a central pool of additional incentives, to drive more efficient use of rezoning and integrated planning.[11]

2.23 The Property Council outlined its position on each funding option in its submission, and argued that while there are a variety of tax options available, 'some will be very harmful and should be avoided'.[12] The Property Council asserted that efficient broad based taxes, productive state debt, asset recycling or user charges are the most efficient ways to fund infrastructure.[13]

2.24 Prosper Australia stressed that the 'funding side of the equation is the crucial element in actually being able to deliver the infrastructure'.[14] The group argued that 'without an update to the funding and financing methodologies and ideas', it was difficult to see how major projects like the Melbourne to Sydney corridor could be progressed. [15]

2.25 The Canberra–Sydney Rail Action Group (C–SRAG) suggested that for specific projects, once the choices between faster and high-speed rail are made, financing decisions will also become clearer.[16]

Private sector investment

2.26 The committee recognises the significant role the private sector plays in infrastructure investment and notes the increases in private sector infrastructure investment in recent decades.

11 Property Council of Australia, *Submission 29*, pp. 13-18.

12 Property Council of Australia, *Submission 29*, pp. 13-18.

13 Property Council of Australia, *Submission 29*, p. 2.

14 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 34.

15 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 34.

16 Mr Robert Bennett, Co-Convenor, Canberra–Sydney Rail Action Group (C-SRAG), *Committee Hansard*, 23 June 2020, Canberra, p. 18.

2.27 Broadly, infrastructure projects funded by the private sector falls into two categories: fully owned and operated by the private sector; and commissioned by government but at least partly financed by the private sector (PPPs).

2.28 PPPs generally involve a long-term contract between the government and a private provider, for the private provider to build and operate an asset or service. Under these arrangements the risk is shared, to varying degrees, between government and private sector project partners, and may involve the private provider taking on management responsibility for the project. The private provider (typically a consortium) usually finances the project.

2.29 PPPs can potentially provide a number of benefits, including: helping to deliver projects on time and at a lower cost over the life of the asset; and from a financing perspective, enabling governments to pursue projects when they are facing short-term fiscal constraints.[17]

2.30 However, in evidence to the committee, Prosper Australia challenged what it saw as the 'over domination by the public–private partnership model of project financing' in recent decades, which it suggested was 'well in excess of the effectiveness of that particular model'.[18] It stated:

> The PPP methodology should always be questioned very rigorously as to whether that's the most cost-effective opportunity and provides the best fund outcomes from a taxpayer's perspective or not. That is a very serious question that really needs to be brought to the table in every major project context, including many in the faster-rail context.[19]

2.31 IFM Investors also raised concerns about the limitations of PPPs, including long and costly bid processes and capital structures that it suggested are 'heavily biased' towards debt. It argued that:

> …especially in respect of large, complex projects, [PPP models] have failed to attract long-term equity investors in any significant way, with shorter-term focused bidding consortia often struggling

17 Chong S and Poole, E, *Financing Infrastructure: A spectrum of country approaches*, Reserve Bank of Australia Bulletin, September Quarter 2013, p. 68.

18 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 32.

19 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 32.

> to effectively manage risks, leading to time and cost overruns or project objectives not being achieved.[20]

2.32 While acknowledging increasing scrutiny of the PPP model for financing rail projects in the United Kingdom, C-SRAG noted that, in contrast, the use of PPPs in financing light rail infrastructure in countries like Canada has been more widely accepted.[21]

2.33 The Queensland Investment Corporation (QIC) highlighted the private sector appetite to invest in rail infrastructure in Australia, pointing to Australia's superannuation system as a key source of investment.[22] IFM Investors also emphasised superfunds' investment in 'delivering major new infrastructure alongside government partners'.[23]

Role for government

2.34 The Australian Government's role in rail projects is not limited to funding. It also has an important leadership role to play in facilitating rail projects, by providing strategic coordination between the different levels of government, the private sector and other key stakeholders. This section briefly covers traditional approaches to funding rail infrastructure and highlights the need for the Australian Government to work with state, territory and local governments, on the integrated planning and land use management—including rezoning opportunities—needed to support rail developments.

Government funding

2.35 The Australian Government has committed to investing $100 billion in transport infrastructure over ten years from 2019-20, with almost a quarter dedicated to rail infrastructure.[24] IPFA and the NFRA noted Macromonitor forecasts that $10 billion in railway construction work will be undertaken annually from 2020 to 2028.[25]

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20 Mr Michael Hanna, Head of Infrastructure, Australia, IFM Investors, *Committee Hansard*, 14 September 2020, Canberra, p. 9.

21 C–SRAG, *Submission 20*, p. 12.

22 Mr Trent Carmichael, Partner, Global Infrastructure, Queensland Investment Corporation (QIC), *Committee Hansard*, 14 September 2020, Canberra, p. 2.

23 Mr Michael Hanna, Head of Infrastructure, Australia, IFM Investors, *Committee Hansard*, 14 September 2020, Canberra, p. 10.

24 IPFA and NFRA, *Submission 8*, p. 10.

25 IPFA and NFRA, *Submission 8*, p. 23.

2.36 Traditionally, major infrastructure projects have been funded by government. As observed by C–SRAG:

> …the Commonwealth has a settled yet flexible and world-class set of financial arrangements and institutions as well as trusted ways of funding large-scale projects. Small-to medium-scale renewal and renovation projects can be readily and securely financed by the Commonwealth on budget and ultimately with a lower borrowing cost than equivalent sums raised privately.[26]

2.37 At public hearings for the inquiry, the committee discussed the application of fiscal policy to funding infrastructure. In response to committee questioning on these broader options, the Newhaven Group agreed that:

> …on the fiscal side, we can print money. We have a hard currency in Australia. The Reserve Bank can print as much money as it likes. We can borrow from the world with ease. We also have our super funds—over $2 trillion in super—that can be deployed in terms of picking up government debt…There's no shortage of debt that we can access at low rates of interest in order to achieve a major infrastructure build in this country.[27]

2.38 Prosper Australia remarked that it was 'encouraged by the willingness to look at fiscal policy like infrastructure bonds and expansionary fiscal policy that currently seems to be happening with the RBA and around the world'.[28] It emphasised that fiscal policy should definitely play a role, particularly in the health and education sectors, where value capture options are more limited.

2.39 In the context of the NFRA advancing business cases on faster rail lines, the Department of Infrastructure, Transport, Regional Development and Communications indicated there will need to be 'a large fiscal contribution from both state and Commonwealth governments to get these projects over the line'.[29]

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26 Mr Robert Bennett, Co-Convenor, C–SRAG, *Committee Hansard*, 23 June 2020, Canberra, p. 18.

27 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 41.

28 Ms Emily Sims, Director of Engagement, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 38.

29 Mr Daniel Caruso, Assistant Secretary, COVID Recovery, Infrastructure Investment Stimulus, *Committee Hansard*, 23 June 2020, Canberra, p. 6.

Cooperation between all levels of government

2.40 The Australian Government plays an important strategic planning role in rail projects beyond that of funding the projects and guiding financing approaches. However, the practical implications of Australia's federal system can mean that delivering these projects involves negotiation and cooperation across all levels of government. For example, where land use planning is shared between different levels of government, or rezoning responsibilities lies with local governments.

2.41 If the Australian Government puts funds into a rail infrastructure project, it will need to negotiate 'how the Commonwealth can get a share of those revenues for the benefit of the Commonwealth taxpayer'.[30]

2.42 The committee heard that there is scope for the Australian Government, working with state, territory and local governments, to build on current mechanisms, like City Deals, when seeking to secure better value sharing outcomes. City Deals are a partnership between the three levels of government and relevant communities, which work to align the planning, investment and governance necessary to accelerate growth and job creation, stimulate urban renewal and drive economic reforms. They are a key mechanism for delivering the Australian Government's Smart Cities Plan.

2.43 The Urban Development Institute of Australia (UDIA) submitted that there is potential through the City Deals approach to 'influence or control land use planning where new major land transport infrastructure is being built'.[31]

2.44 In response to questioning on the topic, Professor McNaughton[32] told the committee that he found the process intriguing, and in his international experience could not 'think of many examples around the world that are as powerful as the city deals process'.[33]

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30 Ms Leilani Frew, Chief Executive, IPFA, *Committee Hansard*, 23 June 2020, Canberra, p. 5.

31 Urban Development Institute of Australia (UDIA), *Submission 23*, p. 3.

32 Professor Andrew McNaughton appeared in a private capacity. His professional background includes more than 45 years working on rail infrastructure projects. Relevant professional roles include: as strategic adviser to the United Kingdom's High Speed 2 project; Chair of the International Railway Union World InterCity and High Speed Forum; and in 2019 leading the expert panel advising the New South Wales Government on how the government should best deliver a fast rail network to connect the state. See <https://www.nsw.gov.au/projects/a-fast-rail-future-for-nsw>, accessed 3 September 2020.

33 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 20.

2.45 Submitters clearly saw a role for government as more than just a funding source for rail projects. Evidence to the committee highlighted the importance of getting the planning right from the start. Value Advisory Partners argued that financing and funding is an integral part of the planning process, and 'not just an add-on at construction or project completion'.[34] Further, it contended that a national approach must include a whole-of-project life perspective, and be applied equally across major urban and regional centres.[35]

2.46 QIC explained that the Australian Government can provide important impetus and certainty for the private sector and other critical players, by bringing together relevant state and local stakeholders to 'cut through…issues at the outset and to try and build a consensus before those projects are taken to the market'.[36]

2.47 Prosper Australia saw the potential for the NFRA to be 'the dominant vehicle through which to achieve strong outcomes on faster rail financing and other issues associated with faster rail'.[37] However, it expressed the view that the NFRA has not yet 'fully teased out' balancing its national level responsibilities and the state-level projects. Prosper Australia contended that NFRA's key responsibilities should encompass:

- stewardship of policy and governance of faster rail issues and acting in the public interest first and foremost
- knowledge management to provide information on international best practice, technical issues, policy issues, and financing and funding issues.[38]

2.48 In its submission, Value Advisory Partners noted conclusions from a 2016 academic study that 'changes in how land is used and valued are better indicators of the benefits of investment in transport than the projected travel time savings which typically are central to the core benefits'. [39]

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34 Value Advisory Partners, *Submission 33*, p. 3.

35 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 51.

36 Mr Trent Carmichael, Partner, Global Infrastructure, QIC, *Committee Hansard*, 14 September 2020, Canberra, p. 5.

37 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 32.

38 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 32.

39 Value Advisory Partners, *Submission 33*, p. 4. Study reference: Metz D, *Travel Fast or Smart? A Manifesto for an Intelligent Transport Policy*, London Publishing Partnership, 2016, University College London.

2.49 In response to committee questioning on the timing for corridor protection of an identified route, Infrastructure Partnerships Australia stated 'the earlier the better', and added that:

> We've seen consistent recommendations from Infrastructure Australia, from the federal government and from other bodies under the High Speed Rail Study in 2014 to say that there is no better time than yesterday to start preserving the corridor, and if we can't do yesterday we should start tomorrow.[40]

2.50 While it would be beneficial—for planning, project delivery and value capture purposes—if government is the primary landowner along a rail corridor, this is unlikely to be the case in Australia. The MTR Corporation described it as a balancing act and commented that for strategic purposes it is preferable for the government to have ownership of certain key locations. It explained that:

> The government will want to acquire and hold on to a bigger piece of land as the anchor for funding purposes or for future sustainable development purposes, but there are some sites where you want to cooperate with existing landowners to create more commercial value and also to add more innovation and creativity in certain sites and parcels of land. So I don't think it has to be entirely government owned land in order for there to be successful projects for faster rail.[41]

2.51 MTR stressed the importance of early planning along a corridor to determine the purpose, density and land uses. From there, governments can then freeze the land uses and focus on the next stage of value capture.[42]

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40 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, pp. 19-20.

41 Mr Terry Wong, CEO, Australian Business, MTR Corporation Limited (MTR), *Committee Hansard*, 21 July 2020, Canberra, p. 7.

42 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 6.

Value sharing

2.52 While there are opportunities for cooperation with the private sector to maximise project opportunities, QIC noted that the private sector does not have 'the resources or the risk appetite to take some of these projects completely off government's hands'.[43] Governments will continue to play a crucial role in funding and facilitating major infrastructure projects, and will need to be savvy when it comes to optimising the use of taxpayer money. When discussing the range of funding options available for infrastructure projects, IPFA commented that:

> We would like to see all forms of funding available to contribute to infrastructure projects—not just government funding but user-pays funding where it makes sense and where it is affordable. We see value capture as another example of user-pays funding. We are not saying that we rely solely upon that, but we do observe that it is an area that has been less developed in Australia than in other areas around the world.[44]

2.53 In their joint submission, IPFA and the NFRA noted that 'value capture mechanisms can assist governments to fund and deliver infrastructure projects on a fairer basis'.[45] However, they cautioned that government must have 'realistic expectations about how much value can be captured'.[46]

2.54 IPFA and the NFRA submitted that, while there was uncertainty about the magnitude of property value uplift, 'a body of evidence does point to increased land and property values for passenger rail at all speeds where there are significant travel time savings'.[47] For example, they cited a Bureau of Infrastructure and Transport Regional Economics survey of land value for more than one hundred passenger rail projects, which showed average uplifts between 6.9 and 9.5 per cent around passenger rail.[48]

43 Mr Trent Carmichael, Partner, Global Infrastructure, QIC, *Committee Hansard*, 14 September 2020, Canberra, p. 5.

44 Ms Leilani Frew, Chief Executive, IPFA, *Committee Hansard*, 23 June 2020, Canberra, p. 6.

45 IPFA and NFRA, *Submission 8*, p. 17.

46 IPFA and NFRA, *Submission 8*, p. 18.

47 IPFA and NFRA, *Submission 8*, p. 18.

48 IPFA and NFRA, *Submission 8*, p. 18.

Rail stations and precincts

2.55 During the inquiry, the committee heard that strategic development of rail stations into a sustainable economic precinct, with connections to the surrounding areas, is an important opportunity to create and capture value.

2.56 The Newhaven Group observed that high-speed rail has been most successful in places like Japan and Taiwan where the private companies operating the rail have also had 'ancillary businesses creating revenue for those companies beyond the fast-rail farebox, most notably in real estate development and commercial real estate operations'.[49]

Entrepreneur Rail Model

2.57 In evidence to the committee, the Newhaven Group referred to the 'Entrepreneur Rail Model',[50] which seeks to harness entrepreneurial skills from the private sector to develop and fund sites for new public transport infrastructure. A discussion paper on the Entrepreneur Rail Model sets out the three-step process as:

- seeing what land use is possible
- getting financing/funding based on this
- estimating transit numbers.[51]

2.58 As noted by the Newhaven Group, this is a reversal of how most transport planning works.[52] The traditional approach in conventional rail models usually starts with estimating transit numbers, follows with getting finance and funding based on these numbers, and lastly, seeing what land use is possible.

2.59 The government's role in the Entrepreneur Rail Model is also significantly different to more traditional value capture methods, and involves:

- land acquisition and assembly
- network coherency and integration

49 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 41.

50 The Entrepreneur Rail model was developed by Professor Peter Newman of the Curtin University Sustainability Policy Institute. House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Harnessing Value, Delivering Infrastructure*, November 2016, p. 178.

51 Curtin University, *Entrepreneur Rail Model: A discussion paper*, Prepared by Peter Newman, Evan Jones, Jemma Green and Sebastian Davies-Slate, February 2016, p. 3.

52 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 40.

- zoning land use changes
- urban development and building standards.[53]

2.60 The Newhaven Group noted that the model involves predicting how much land can be developed as the fundamental source of funding, and then producing an estimate of potential transit patronage to match a fit-for-purpose infrastructure design. It argued that:

> …this is the best way for Australia to deliver fast rail on the east coast. Population management and spatial settlement must come first, and it must be done with a mind to creating enough uplift in values that can be extracted to fund most, if not all, of the capital costs of the infrastructure.[54]

Rail plus property model

2.61 The MTR Corporation's approach in Hong Kong involves using the profit from sales of fully developed assets to fund infrastructure costs for the project. Under the Rail plus property model:

- rail projects are assessed in terms of their capital and operating costs over the life of the line
- revenue is estimated and the gap between the two identified
- development rights are assessed and used to fill the funding gap, with a land premium going to the government to pay for this development right
- in conjunction with private developers, MTR invests in property development in and above the station precinct, creating an ongoing profit stream.[55]

2.62 The benefits to the Hong Kong Government include a free transport service, the land premium from lease of land, and an ongoing dividend from MTR's profit. The rail and property projects are implemented together in a coordinated way creating multiple uses of the same land; station areas including offices, shopping and residential within the airspace covering the station footprint. The outcome is rapid and

53 House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Harnessing Value, Delivering Infrastructure*, November 2016, pp. 178-179.

54 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 40.

55 House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Building Up & Moving Out*, September 2018, p. 407.

coordinated development of infrastructure and commercial and residential space.[56]

2.63 MTR told the committee that, since opening its first line in 1979, it has used the rail plus property model 'to fund the construction and operation and maintenance and upgrade of the railway lines and make it work efficiently'.[57]

2.64 MTR explained that comprehensive planning is needed at the broader strategic level, for instance factoring whole city planning, then at the district level and the precinct level. To turn a location into a transport hub and business precinct you must begin with a rail station and then station development, which can include connectivity to the neighbouring area.[58]

2.65 The NFRA and IPFA noted that the MTR Rail plus property model depends on low cost land and air rights along rail corridors, which can 'subsequently be developed into high density, high value, residential and commercial space and used to offset the cost of rail infrastructure'.[59] They clarify that this is possible in Hong Kong due to government land ownership.

2.66 While the Australian context does not readily offer the key underlying benefits that come with broader government land ownership and high population density, as is the case in Hong Kong, MTR contended that the model has application for rail projects in Australia. It stated:

> Once you have the high-speed rail there, you're able to support higher density uses. Of course you won't have such high density as you see in Hong Kong, but still you will find a balance…Even if you can't recoup the capital costs, but it can help paying for the maintenance, operating and upkeep costs.[60]

2.67 MTR acknowledged that the best rail alignment for transport purposes may have to be balanced against land availability, the best alignment for urban planning purposes, and timing considerations. It stated that:

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56 House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Building Up & Moving Out*, September 2018, p. 407.

57 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 2.

58 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 2.

59 IPFA and NFRA, *Submission 8*, pp. 18-19.

60 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 6.

> If government land is available at different places, you may have to shift the alignment a little bit or you may have to shift the station a little bit, in order that the railway corridor can be built together with the development corridor in the time frame intended.[61]

2.68 It was noted in the Environmental Impact Statement Summary for the development of the rail in the Sydney Metro Western Sydney Airport project that existing government owned land is being used, where possible, to avoid acquiring private land. However, the project will include 'around 28 full property acquisitions, 33 partial property acquisitions and 11 temporary leases'.[62] The planned acquisitions will be undertaken in accordance with the New South Wales *Land Acquisition (Just Terms Compensation) Act 1991.*

2.69 While acknowledging there was no set rule for the size of the precinct or area impacted by a new railway station, MTR suggested that a 500 metre walking catchment was the 'general rule of thumb' for government to pay attention to in providing good pedestrian connection. This will differ in the case of a greenfield site, where more government planning is required in using rail as the catalyst to move jobs and people to the area.[63]

2.70 MTR outlined that in its Hong Kong projects, it prepares a master plan for the identified precinct, which could range from two or three hectares (20,000 or 30,000 square metres) to its largest 32 hectare (320,000 square metres) precinct at LOHAS Park in Hong Kong. The plan is then approved by the town planning board. In terms of packing land parcels and planning precincts around rail stations, MTR stated:

> Usually, when we do the site delineation, we may call it a small precinct—the station is already one hectare, including the facilities—and then we include the areas around it. In Hong Kong, it's very common to have a transport interchange right next to the station.[64]

61 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 3.

62 Australian Government, New South Wales Government and Sydney Metro, *Environmental Impact Statement Summary*, October 2020, p. 38.

63 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 5.

64 Mr Steve Yiu, Principal Advisor, Town Planning, MTR, *Committee Hansard*, 21 July 2020, Canberra, p. 5.

Just, equitable and fair portion

2.71 During the inquiry the committee explored what might constitute a 'just, equitable and fair' portion of value sharing between beneficiaries and government. In their joint submission, IPFA and the NFRA explained that:

> The willingness to pay a value capture contribution is directly related to the perceived fairness of the model, the amount, hypothecation [allocation of tax revenue to particular expenditure] and whether an individual recognises personal benefit from the infrastructure delivered. Given the potential for value capture to make a contribution to the funding mix, there would be merit in a broader conversation between all levels of government and the community about the willingness and appropriateness of value capture mechanisms.[65]

2.72 Submitters generally supported the principle of value sharing where the government's investment in infrastructure is the major contributing factor to substantial increases in property values. However, determining a specific percentage, portion or capped amount requires thorough examination and negotiation between government and key stakeholders.

2.73 In response to committee questioning, Professor McNaughton said that it was not his role to suggest what proportion is fair or unfair. However, a reasonable balance between taxpayer and current landowners could be found, 'whether it is 50 per cent or 75 per cent, that is massively different to the nought per cent you will get if you do not act'.[66]

2.74 Arup stressed the importance of forward-notice for affected parties. It suggested that there should be a standard device for the government to: announce the infrastructure; flag that, for example, a development level framework will be imposed in the area; and explain that this means that the owner's land is 'crystallised or realised at value' and that the Australian Government will be taking a certain share of the value generated by the new infrastructure.[67]

65 IPFA and NFRA, *Submission 8*, p. 4.

66 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 20.

67 Dr Timothy Williams, Australasian Cites Lead, Arup, *Committee Hansard*, 23 June 2020, Canberra, p. 50.

Value capture mechanisms

2.75 Prosper Australia contended that 'value capture streams can provide the repayment opportunity over time with greater stability and reliability'.[68] Value Advisory Partners observed that value capture mechanisms are 'more likely to be successful and sustainable if they are implemented within a structured policy framework, rather than in an ad hoc manner'.[69]

2.76 Value creation and capture mechanisms are not new and have been used internationally for many years. Value Advisory Partners noted that in Australia, value capture mechanisms have been used since the 1920s with the Sydney Harbour Bridge.[70]

2.77 In terms of the property industry, the Property Council highlighted that the different levels of governments already receive taxes that capture some degree of economic uplift at the:

- Australian Government level—including company tax, capital gains tax and the goods and service tax (GST)
- state or territory level—including stamp duty, payroll tax and land tax
- local government level—including rates, fees and charges.[71]

2.78 Infrastructure Partnerships Australia supported a broad based land tax for capturing value and encouraging 'highest and best use on developments'.[72] It emphasised that, in contrast to other approaches discussed, a substantial advantage of this approach is that other methods depend on early action, because once speculation occurs, 'the horse has already bolted' for capturing uplift.[73]

2.79 The Newhaven Group outlined three major financing pillars: seed capital or down payment available; collateral or security that can be provided to financiers; and ongoing cash flow of the particular asset investment. In the context of high-speed rail in Australia, the group commented that:

> …in the absence of land value capture we would see either the government printing money or borrowing money and committing

68 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 5.
69 Value Advisory Partners, *Submission 33*, p. 14.
70 Value Advisory Partners, *Submission* 33, p. 14.
71 Property Council of Australia, *Submission* 33, p. 7.
72 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 17.
73 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 17.

> themselves to years of subsidies being paid to run the rail until the farebox had reached a stage where it was able to cover the operational cost of the rail itself.[74]

2.80 In exploring funding options for transport projects proposals, IPFA and the NFRA recommended considering:

> …what proportion of the project can be funded by the key beneficiaries of the project through targeted contributions and farebox recovery, and how much should be funded by the broader community?[75]

2.81 The discussion in the following subsections will cover the tax increment financing model as an indirect value capture option. Then at the state and territory levels—the Victorian Value Creation and Capture Framework, and the Lease Variation Charge in Canberra—and rezoning, as opportunities for value capture.

Tax Increment Financing

2.82 The United States tax increment financing (TIF) model involves raising financing against future tax revenue, by identifying the business-as-usual taxes in the area prior to the infrastructure investment and then estimating the uplift in tax revenue values in a declared area directly affected by public infrastructure projects. The increase in tax revenue from the uplift in property values can then be directed towards funding the project.[76]

2.83 The UDIA submitted that TIF merited consideration, as a complement to asset recycling and public private partnership approaches.[77]

2.84 The Property Council advocated for TIF, which is used primarily at the local and state levels. It contended that TIF can be a potential partial funding source for rail and other improvement projects. Further, it commented that this type of approach aligns different parties, including government planning agencies with infrastructure providers, developers and the local businesses and residents.[78]

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74 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 40.

75 IPFA and NFRA, *Submission 8*, p. 21.

76 Mr Kenneth Morrison, Chief Executive, Property Council of Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 12.

77 Mr Simon Basheer, National President, Urban Development Institute of Australia, *Committee Hansard*, 21 July 2020, Canberra, p. 16.

78 Mr Kenneth Morrison, Chief Executive, Property Council of Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 8.

2.85 However, Infrastructure Partnerships Australia argued that TIF does not apply in the Australian content 'because it solves a problem we don't have and it introduces complexity that we don't need'.[79] Infrastructure Partnerships commented that in Australia it is possible to raise finance at very cheap relative rates, particularly in the current context with relatively cheap borrowing rates for government.[80]

Victorian Value Creation and Capture Framework

2.86 Value Advisory Partners commented that current approaches in Australia 'tend to provide only moderately recoverable revenue streams', which has meant a reliance on government investment and funding.[81] However, it noted that Victoria was the exception, with the state adopting a value creation capture framework in 2016, and 'actively seeking business cases to integrate monetisable benefits alongside traditional social, productivity, connectivity and system-wide benefits'.[82]

2.87 The Victorian Government's Value Creation and Capture (VCC) Framework sets out a consistent, concerted approach to assessing and increasing the economic, social and environmental benefits of investments in Victoria, including in the transport, health, housing and education sectors. The VCC Framework provides a menu of mechanisms for project sponsors to consider using in projects. Its stated focus is getting better value for Victorian taxpayers' money from all future infrastructure projects.[83]

2.88 Value Advisory Partners noted that the Victorian framework directly identifies benefits that generate additional revenue streams.[84] It submitted that the advantages of the value and creation approach for rail projects would be:

- it identifies additional opportunities which will allow for a broader set of benefits and beneficiaries

79 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 18.

80 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 18.

81 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 51.

82 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 51.

83 Victorian Government, *Value creation and capture framework*, <https://www.vic.gov.au/value-creation-and-capture-framework>, accessed 5 November 2020.

84 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 51.

- the benefits can be localised and are additive
- the benefits are quantifiable and directly attributable to beneficiaries
- through the identification of mechanisms that target specific benefits for beneficiaries, value can be directly realised and used to contribute to funding infrastructure
- there is no double counting of benefits.[85]

2.89 *Victoria's Value Creation and Capture Guidelines*[86] sets out the steps in the VCC process. It notes that for government to make an investment decision, details of the costs and benefits of each VCC mechanism are needed. It identifies the broad range of benefits as:

- Core project benefits: Value delivered from core project.
- Wider economic benefits (WEBs): Economic assessment of wider economic benefits for user benefits – metro/ state wide, productivity and liveability.
- Benefits created or captured by VCC mechanisms (VCC benefits): Value created due to the project and additional opportunities delivered (property, amenity, social, environmental, cultural opportunities).[87]

2.90 Value Advisory Partners noted that the Victorian VCC mechanism framework was the 'first time we have seen in policy in Australia where a government has actually dictated that infrastructure provides new value, and new value is where that capture should come from'.[88]

ACT Lease Variation Charge

2.91 In the Australian Capital Territory, a 75 per cent Lease Variation Charge (LCV) is applied when a lease holder received permission to vary their lease to enable new or additional development.[89]

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85 Value Advisory Partners, *Submission 33*, p. 10.

86 *Victoria's Value Creation and Capture Guidelines* provide direction for: departments and agencies on how to investigate and identify broader VCC opportunities for government investment; and project sponsors and delivery and advisory agencies on how to comply with the VCCC Framework requirements.

87 Victorian Government, *Victoria's Value Creation and Capture Guidelines: Information for precincts, development of public land and capital investments*, 31 August 2018, p. 19.

88 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 53.

89 In the Construction Sector Recovery Package—as part of the COVID-19 recovery phase—the ACT Government announced on 25 June 2020 that developments requiring a lease variation may be eligible for a 50 per cent reduction (capped at $250,000) in the LVC for a limited time.

2.92 Mr Skinner cited a submission to a current New South Wales Productivity Commission inquiry into infrastructure, which claimed that if the ACT LVC—75 per cent betterment levy—had been applied, it would have generated $8 billion in NSW, and $18 billion nationally. While he noted that this is not solely related to transport infrastructure, it 'gives a taste' of what is possible with this type of approach.[90]

2.93 In discussing the potential application of a similar approach more widely, Prosper Australia stated that the 75 per cent LVC is taken in the ACT with 'no real impact on the market'. [91]

Rezoning opportunities

2.94 Mechanisms like the ACT LVC rely on having arrangements in place linked to rezoning. The inquiry included discussion of rezoning opportunities for value capture.

2.95 Professor McNaughton stated that 'preferably every time you rezone you capture something'.[92] This will help contribute to asset management of the new railway and potentially towards subsidising fares.

2.96 In the case of a new rail station, this could involve making the rezoning contingent on a legally binding agreement that at least a proportion of the resulting uplift is 'captured or paid back to the public sector at various stages in the development'.[93] Professor McNaughton stressed that the opportunity for value capture is lost if the zoning is changed without an agreement in place.

2.97 In discussions on how far the precinct around a rail stations could be affected, Professor McNaughton noted that the 'sweet spot' tends to be within 500 metres around a station. However, development uplift could potentially extend much further to four or five kilometres beyond the station.[94]

2.98 When discussing the potential application for capturing value from wider developments, such as housing in the extended precinct, Professor McNaughton commented that:

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90 Mr Steve Skinner, *Committee Hansard*, 17 August 2020, Canberra, p. 4.

91 Ms Emily Sims, Director of Engagement, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 36.

92 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 19.

93 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 18.

94 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 17.

> …around the world the public sector is not very good at doing hard commercial deals with property developers. They tend to drive a very hard bargain by threatening not to develop—and the public sector too often blinks first.[95]

2.99 Prosper Australia observed that the initial rezoning and associated large-scale uplift created purely from an infrastructure project is an area that 'is getting away from us the most in Australia and is doing the most damage'.[96]

2.100 The Property Council noted that in most jurisdictions in Australia, there is some sort of contribution linked to major rezoning arising from infrastructure projects. It stressed the need to get the alignment right and cautioned that sometimes these contributions are 'calibrated too high and act as a handbrake on the development going forward'.[97]

2.101 Value Advisory Partners recommended that the Australian Government 'consider developing, promoting and implementing a national value capture framework, designed to ensure national consistency and reduce any anomalies between different states and territories'.[98] It proposed that the national value capture framework be piloted alongside traditional cost-benefit and economic impact assessments.

Value sharing considerations and limitations

Missed opportunities for sharing value uplift

2.102 During the inquiry, the committee considered whether gaps in the current mechanisms allow for value escape where major infrastructure projects are contributing to significant increases in property values. Value escape refers to public spending on infrastructure that directly leads to private benefits that are not shared by government.

95 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 18.

96 Dr Chris Hale, Consultant, Prosper Australia, *Committee Hansard*, 23 June 2020, Canberra, p. 36.

97 Mr Kenneth Morrison, Chief Executive, Property Council of Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 9.

98 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 51.

2.103 Value Advisory Partners submitted that current financing delivery models have understated the potential for beneficiary value capture 'at an average of 80 to 90 per cent', which means that 'as much as 5 to 10 times the value that could be used for funding and financing escapes'.[99] In the context of fast rail projects, Value Advisory Partners recommended that:

> …fast-rail project appraisals be required to consider alternative funding and financing options that link contributions from beneficiaries to the benefits that would be received from the delivery of the projects; and that the implementation of the fast-rail proposals should be integrated with any land rezoning or land use developments, to optimise the potential opportunities for value capture and minimise value escape.[100]

2.104 It has been reported in the media that the airport development at Badgerys Creek has resulted in significant increases in land values in the area. For example, a property in Martin Road was reported to have sold for 84 per cent higher than the last suburb record, with a two hectare site sold to investors for $5.75 million.[101]

2.105 During the inquiry, the airport site at Badgerys Creek[102] was discussed as an example of where landowners had already made '"huge" unearned gains on the back of the government infrastructure decisions and planning commitments'.[103] In his submission, Mr Steve Skinner[104] contended that with the approximately $20 billion government investment flagged in the western Sydney airport area 'you didn't have to be Einstein to realise that land values would take off'.[105]

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99 Value Advisory Partners, *Submission 33*, p. 1.

100 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 51.

101 *Australian Financial Review*, 'Badgerys Creek land sales soar', 25 October 2018, p. 47.

102 The Western Sydney City Deal will drive the development of the Western Sydney Airport and Badgerys Creek Aerotropolis. See < https://www.greater.sydney/metropolis-of-three-cities/productivity/jobs-and-skills-city/western-sydney-airport-and-badgerys>, accessed 16 November 2020.

103 Mr Steve Skinner, *Submission 34*, p. 11.

104 Mr Steve Skinner provided evidence to the committee in a private capacity. He produced an academic paper as part of the Henry Halloran Trust at the University of Sydney entitled *Value Capture on Urban Road and Rail Projects: Are There Too Many Free Rides?*, July 2019. Mr Skinner has worked as a journalist of many years, including with Fairfax, the Australian Broadcasting Corporation and Bauer Transport Media. See <https://www.sydney.edu.au/henry-halloran-trust/about/our-people.html>, accessed 3 September 2020.

105 Mr Steve Skinner, *Submission 34*, p. 10.

2.106 When questioned by the committee on what lessons can be learned from the Badgerys Creek development, Arup responded that it is a:

> …shocking example of the public sector creating disproportionate private uplift that has been pocketed by individuals. The community thinks that's not equitable and it doesn't strike anyone as sensible…I believe there's community consensus for saying 'If the public sector creates that amount of value, why can't we share in that to help us fund the infrastructure in the first place?' [106]

2.107 While not linked to a specific infrastructure project, the Newhaven Group gave an example of the impact of rezoning on a block of land in the west of Melbourne where a lot increased in value from $1,750 to $31,500, or '$25,000 a hectare to $350,000 a hectare just on the promise of rezoning in the future'. [107]

2.108 The Newhaven Group posited that, in the context of property value increases arising from rail infrastructure, it is reasonable for something to be extracted to contribute to the infrastructure. Using the above case to illustrate the point, the Newhaven Group observed that:

> At the moment all of the value I just described goes to the farmer, who's basically won TattsLotto for owning a farm on a piece of land that the planners have decided to rezone for housing as the city has grown. He'll pay capital gains tax on it if he's owned it post-1985, but there's no more extraction from it. The rest of the value that is extracted is down the track. It's extracted once the developers own it.[108]

2.109 In his submission, Mr Skinner set out a number of cases studies that he deemed to be missed opportunities, where significant windfalls were involved.[109]

Timing considerations

2.110 A recurring theme in evidence to the committee was that speculation on property value uplifts linked to potential infrastructure projects starts early. Consequently, by the time plans are in place and a project is announced, it is likely that the horse has already bolted on opportunities

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106 Dr Timothy Williams, Australasian Cites Lead, Arup, *Committee Hansard*, 23 June 2020, Canberra, p. 48.

107 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 42.

108 Mr Jay Grant, Partner, Newhaven Group, *Committee Hansard*, 23 June 2020, Canberra, p. 42.

109 Mr Steve Skinner, *Submission 34*, pp. 4-19.

for the government to capture value uplifts on property in the rail precinct and along the rail corridor.

2.111 Evidence reflected that exploring value capture options cannot be an afterthought and must feature as an integral part of project planning. Professor Andrew McNaughton told the committee that 'land value starts to rise the moment a government announces its intention to build a network or line or a station'.[110] Mr Skinner described the current sequencing in Australia as 'back to front' and stated that:

> …first, master plans are announced and then various other stages, and then, right at the end, finally, governments get around to announcing some sort of value capture funding mechanisms, assuming you want to include special infrastructure contributions as value capture.[111]

2.112 Similarly, Value Advisory Partners stressed the need for a value capture framework to be in place at the planning stage, and to have a clear understanding of the maximal amount of value that can be achieved through these projects.[112]

2.113 Value Advisory Partners also cautioned about the impact of early announcements of projects, even where specific rail stations are not identified. It contended that these announcements can have a significant effect on the ability of governments to capture uplift:

> People start speculating and buying properties. They build apartments and infrastructure through there and see what the outcomes can be. We have to be careful about announcements being made too early, because, without the appropriate mechanisms in place, they can actually diminish the ability of governments and other groups to recover the revenues…
>
> But, yes, sometimes the horse has bolted, as you say: $11.5 billion, and there's a station going from St Marys to the airport. I think a lot of people could actually go back and draw a line. There are pretty easy rules of thumb: draw a straight line, don't cross any roads—they'll put a bridge over them—try and make sure there's

110 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 16.

111 Mr Steve Skinner, *Committee Hansard*, 17 August 2020, Canberra, p. 3.

112 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 56.

> two kilometres between each station, and you'll know where most of your stations are going to be.[113]

2.114 Professor McNaughton provided an example in Birmingham in the United Kingdom to emphasise that if you leave value capture until after a new rail station is announced, 'the capture has gone'.[114] In this case, the government announced the site of a new station before it had passed the supporting legislation covering the station's location and what it would comprise.

Value capture limitations

2.115 A number of submitters expressed reservations about the use of value capture mechanisms. For example, they noted that existing taxes already capture uplift in land values and from economic activity, such as: company tax, capital gains tax and GST paid to the Australian Government; stamp duty and land tax paid at the state or territory level; and rates, fees and charges paid at the local government level.[115] UDIA cautioned against adding an additional burden 'without effectively rebalancing the tax mix portfolio'.[116]

2.116 The Property Council emphasised that property value uplift is already captured by existing taxes, and stated that there is already a significant burden placed on property and property developers—particularly new development—with the property sector contributing 16 per cent of the nation's tax bases with payments of over $72 billion in revenue to federal, state and local governments. It outlined that the highly taxed property industry paid: $21 billion in taxes to Australian Government; $27 billion to the states; and $23 billion to local governments in rates, fees and charges.[117]

2.117 When questioned on missed opportunities for capturing value uplift, and whether stamp duty is capturing sufficient value where there are sizable property value increases due to infrastructure projects, Infrastructure Partnerships Australia responded that 'based on the current paradigms

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113 Mr John Marinopoulos, Partner, Value Advisory Partners, *Committee Hansard*, 23 June 2020, Canberra, p. 54.

114 Professor Andrew McNaughton, *Committee Hansard*, 14 September 2020, Canberra, p. 21.

115 Property Council of Australia, *Submission* 33, p. 7.

116 Mr Simon Basheer, National President, UDIA, *Committee Hansard*, 21 July 2020, Canberra, p. 17.

117 Property Council of Australia, *Submission 29*, p. 7.

we're not missing out'.[118] However, it did concede that there is scope for more to be captured:

> Absolutely; if there are substantial windfall gains, we as taxpayers should be benefiting more from that. But who in that chain pays doesn't change the fact that the taxpayer has captured some of that value. Have they captured enough? Potentially not; but just because it is the developer rather than the speculator doesn't mean it hasn't been captured.[119]

2.118 In relation to stamp duty collected, IPFA observed that as an indirect tax arrangement there is no guarantee that the tax revenue collected will be allocated to infrastructure.[120] In practical terms, this means that where there have been significant property value increases arising from Australian Government funded infrastructure projects, the stamp duty collected from owners benefiting from the value uplift will typically go back into consolidated revenue funds, and not necessarily directed to funding the specific project that caused the uplift or to infrastructure spending more generally.

2.119 Infrastructure Partnerships Australia stated that value capture for faster rail projects can, and should, be considered, but that 'this contribution is likely to be a minor part of the broader project funding mix required for major projects of this nature'.[121] Further, it argued that a project should be selected on its merits, and that selecting a project based on 'its potential to harness value capture is putting the cart before the horse'.[122]

2.120 Arup commented that, in its experience, 'value capture generally contributes a relatively small proportion of the total capital cost of a rail project', which in the case of the Cross Rail in London contributed about 14 per cent towards the project cost.[123] Infrastructure Partnerships similarly observed that value capture contributions are 'likely to be a

118 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 16.

119 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 16.

120 Ms Leilani Frew, Chief Executive, IPFA, *Committee Hansard*, 23 June 2020, Canberra, p. 3.

121 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 15.

122 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 15.

123 Arup, *Submission 17*, p. 6.

minor part of the broader project funding mix required' for major rail projects.[124]

Value creation and capture recommendations by previous committee

2.121 This is not the first time that the committee has heard evidence regarding the benefits of value capture. In the last parliament, two reports by the previous committee examined value capture mechanisms as a way to equitably capitalise on taxpayer funds invested in infrastructure projects.

2.122 A number of recommendations in the *Harnessing Value, Delivering Infrastructure* report[125] included value creation and value capture themes, for example:

- That the Australian Government:
  - ⇒ in conjunction with state and territory governments, develop a framework for the specification and evaluation of proposals for the development of a high speed rail network in eastern Australia, with an emphasis on strategic decentralisation, regional economic development, value creation and value capture to determine the viability of private sector proposals, routes, schedule for development and funding for the project (Recommendation 2)
  - ⇒ investigate options for private funding of high-speed rail through value capture (Recommendation 3)
  - ⇒ recognise the potential contribution towards the costs of new transport infrastructure of the capture of increased property values and associated taxes that directly result from the new connectivity (Recommendation 7)
  - ⇒ seek a memorandum of understanding to establish value capture mechanisms for individual transport projects as a condition of federal funding which applies to property value uplift that results from a combination of rezoning and new transport infrastructure (Recommendation 10)
  - ⇒ develop value capture models that can be applied to major infrastructure projects (such as high speed rail), seek to negotiate

124 Mr Adrian Dwyer, CEO, Infrastructure Partnerships Australia, *Committee Hansard*, 17 August 2020, Canberra, p. 15.

125 House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Harnessing Value*, *Delivering Infrastructure*, November 2016, pp. xix-xxiii.

with the states and territories a consistent and coordinate approach to the application of value capture for such projects, and be prepared to act as the single point for the collection of value capture revenues. (Recommendation 13)

- That the Department of Infrastructure and Regional Development, in conjunction with state and territory governments, develop a toolkit of value capture mechanisms that can be applied at all levels of government. (Recommendation 11)
- That one of the elements of the City Deal-type agreements should include drawing on the proposed value capture toolkit to defining the value capture mechanisms that will be applied, and determining the amount of uplift that can be captured. (Recommendation 12)

2.123 In its March 2018 response to the *Harnessing Value, Delivering Infrastructure* report, the Australian Government noted a range of initiatives announced that directly related to the recommendations. Further, as part of becoming a more informed investor, the Australian Government indicated it was exploring value capture and user-charging as alternative funding streams.

2.124 While the Australian Government cautioned that 'value capture is not a panacea to addressing funding shortfalls for major projects', and is not necessarily applicable to all projects, it noted that it has started implementing its value capture policy through its engagement with state and territory governments on major transport infrastructure projects.[126]

2.125 In the *Building Up & Moving Out* report, September 2018, the previous committee recommended that the:

> …Australian Government develop a system of value capture as an organising principle of infrastructure planning and procurement, and progress the reform of the taxation system to match the requirements of value capture, in conjunction with State and Territory Governments, to provide a single, seamless, transparent system of taxes, charges and contributions, which allows for the costs of infrastructure development, where appropriate, to be met on the beneficiary pays principle.[127]

126 Australian Government, *Australian government response to the House of Representatives Standing Committee on Infrastructure, Transport and Cities: Harnessing Value, Delivering Infrastructure*, March 2018, p. 3.

127 House of Representatives Standing Committee on Infrastructure, Transport and Cities, *Building Up & Moving Out*, September 2018, Recommendation 37, p. 408.

2.126 In the Australian Government's response to that report, it noted this recommendation and commented that issues raised in the recommendation were addressed in the government response to the *Harnessing Value, Delivering Infrastructure* report. It also noted that IPFA supports the Government's infrastructure investment decisions, including through investigating and advising on opportunities for value capture.

Committee comment

2.127 Major infrastructure projects, including rail projects, are important economic enablers. The committee notes that almost a quarter of the Australian Government's $100 billion investment in transport infrastructure will be dedicated to rail infrastructure.[128]

2.128 It is crucial that the Australian Government take a leadership role in maximising opportunities for projects already identified, and in strategic planning for future projects. Major transport projects can lead to significant uplift in property values within the vicinity of the project, particularly near a new rail station or along the rail corridor.

2.129 The committee sees value sharing as complementing broader fiscal policy approaches, and acknowledges that value capture is only one part of the toolkit of financing and funding options for infrastructure projects. There are a complex range of factors that can contribute to increases in land values, and value capture opportunities can vary and must be explored on a project-by-project basis. However, evidence to the committee indicated that while value capture is considered as part of business cases, it is underdeveloped in Australia.

2.130 The committee notes that in the March 2018 government response to the *Harnessing Value, Delivering Infrastructure* report, the Australian Government at the time did not agree with using the potential for value uplift as a factor when prioritising infrastructure projects.[129] The committee believes this position should be reconsidered, especially during this time of economic recovery.

128 IPFA and NFRA, *Submission 8*, p. 10.

129 Australian Government, *Australian Government response to the House of Representatives Standing Committee on Infrastructure, Transport and Cities: Harnessing Value, Delivering Infrastructure*, March 2018, pp. 20-21.

2.131 Value capture is a means by which governments can fund part, or all, of the costs of infrastructure projects, and in time achieve profitable outcomes. It is regrettable that in cases like the Western Sydney City Deal, governments have failed to value capture extraordinary uplifts in property values in the area.

2.132 When Australian Government funded infrastructure is clearly and directly linked to extraordinary value uplifts, or rezoning, governments have a duty to taxpayers to secure a just, equitable and fair portion of these increases in value. What constitutes a 'just, equitable and fair' portion and determining specific percentages or caps will require thorough examination and negotiation between governments at all levels and key stakeholders.

2.133 Early action and integrated planning is crucial. Value capture should be part of the conception of all infrastructure projects, to ensure that governments can equitably capitalise on taxpayer funds invested. It should be incorporated organically into the planning and development of projects, with suitable value capture mechanisms being identified and applied from the outset.

2.134 Value capture mechanisms should also include a method of calculation and equitable apportioning of the value capture. In addition, it should include the estimated funding expected to be generated from the government's portion of the value share, which will go towards paying for the relevant project, and so reducing the burden of debt payments on taxpayers.

2.135 During the inquiry, the committee was disappointed to hear about a number of instances of significant value escape in recent years. Immediate action is needed to prevent further missed opportunities for value sharing. The Australian Government, in consultation with state, territory and local governments, should develop and implement a framework to facilitate value sharing without further delay.

Recommendation 1

2.136 **The committee recommends that the Australian Government, in consultation with state, territory and local governments, develop mechanisms at the national level for value capture of uplifts in property values relating to rail infrastructure projects, wholly, or partially, funded by the Australian Government.**

Recommendation 2

2.137 **The committee recommends that the development of mechanisms for value capture of land value uplift resulting from wholly, or partially, Australian Government funded rail infrastructure projects should consider and determine:**

- **how mechanisms that utilise rezoning opportunities, such as the Australian Capital Territory Lease Variation Charge, could be applied more broadly**
- **what constitutes a 'just, equitable and fair' portion of uplift to be shared between taxpayers and beneficiaries, and what, if any, caps could be applied**
- **how the value share received can be quarantined, allocated fairly between the levels of government, and used for relevant infrastructure projects**
- **options for streamlining value capture payments, to avoid unreasonable duplication, for example through a secondary developer levy if already captured from the landowner's value uplift**
- **how access to Australian Government funding will be conditional on meeting the set criteria.**

2.138 The committee also sees identifying and locking in base land values as a crucial early step to enable value sharing in the significant property value uplift generated from a wholly, or partially, Australian Government funded transport infrastructure project, such as rail projects.

2.139 However, the committee notes the importance of clearly communicating these changes and protecting the interests of landowners and affected parties. For example, if—as proposed in the below recommendation—a mechanism is adopted to secure base land values prior to development announcements and rezoning, this should be clearly communicated to stakeholders.

Recommendation 3

2.140 **The committee recommends that the Australian Government, in consultation with state, territory and local governments, establish a mechanism to secure the base value of land that can be reasonably expected to receive value uplifts resulting from a rail infrastructure project that will be wholly, or partially, funded by the Australian Government. This mechanism should be applied early in the planning stage and in advance of any project announcements.**

John Alexander OAM MP
Chair
4 December 2020