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14 December 2007

Mr. Lyndon Rowe
Inquiry on Developer Contributions to the Water Corporation
Economic Regulation Authority
PO BOX 8469
Perth Business Centre
PERTH WA 6849

By email: developercontributions@era.wa.gov.au

Dear Mr. Rowe

INQUIRY INTO DEVELOPER CONTRIBUTIONS TO THE WATER CORPORATION

The Urban Development Institute of Australia (UDIA) (WA) is pleased to offer the following comments on the ERA issues paper, *Inquiry into Developer Contributions to the Water Corporation* (the Inquiry). UDIA (WA) is the peak body representing the property industry in Western Australia and our members make significant contributions to the Water Corporation for headworks in order to supply water to new residential developments.

Relevant to this inquiry are the recent changes Water Corporation introduced on bonding and UDIA's response is included as Attachment 1.

The section of the submission addresses UDIA members' response to the Inquiry's Terms of Reference:

1. General principles

UDIA (WA) strongly supports the current uniform headworks charge that the Water Corporation applies to residential developments across Western Australia and industry is of the firm opinion that the system should not be changed in any way. It is imperative that the current cost approach of calculating a per lot fee for major works continues as it provides certainty to the development industry which allows relatively accurate costs to be factored into project feasibilities and ongoing developments.

The development industry understands that Water Corporation has to charge for headworks but it is imperative that it remain a uniform charge and that it is not overcharged. The financial viability of many developments hinges on the costs of infrastructure and it is important that the developer establishes known costs prior to the commencement of a project to reduce risk and to provide certainty to the market. This is particularly pertinent in the current climate of declining

housing affordability and strong population growth that is projected to continue for the next decade so that the release of new land to the market is delivered efficiently and cost effectively.

UDIA (WA) is totally opposed to the introduction of headworks charges that follow the Western Power model which was recently introduced in the South West Integrated System (SWIS) which in our view discriminates heavily against regional development. Within weeks of the introduction of locational based headworks charges by Western Power, residential development in Walpole has ground to a halt as projects are rendered unviable due to the impact of prohibitive costs of headworks. Walpole is just the first reported casualty of the system and the first of many projects that will not be completed or commenced because of the impost of unrealistic infrastructure charges. There will be a cumulative negative effect on the economic and social development of the SWIS as small to medium enterprises can no longer afford to set up businesses in the region. The flow on effect will be to stymie town centre development, employment growth, service industry growth and residential development in regional areas. These impacts would be further exacerbated were Water Corporation also to apply non-uniform headworks charges.

Uniform headworks charges are reflective of the integrated nature of the scheme in WA. UDIA believes this is an equitable approach which does not discriminate against areas outside the Perth Metropolitan Area or non-urban areas outside regional centres. The ongoing resource boom continues to put substantial growth pressures in regional areas and significant financial impediments to regional growth need to be eliminated.

UDIA would like greater transparency around Water Corporation's total revenue streams to ensure that the current, as stated 40% recovery of infrastructure costs being levied to developers, on a per lot basis, is fair and equitable. Industry would like greater clarity on the 40% / 60% expenditure breakdown and suggest that ERA investigate how money raised from charges is spent, that is the proportion of monies spent on infrastructure construction, investment, maintenance and profit paid to State Revenue. Greater transparency is needed to ensure the Water Corporation is operating and investing sufficiently in the maintenance of infrastructure, and also that water consumption tariffs levied on home occupiers are fair and equitable. UDIA wishes to continue its participation in the ongoing setting of charges as it currently is through UDAC.

2. Efficiency of standard headworks charges

UDIA takes issue with the statement:

'alternative pricing structures have the potential to encourage more efficient urban development through cost reflective price signals'.

Water is only one of many drivers influencing where and when urban development occurs and it goes against proper and orderly planning to use a price signal for one commodity to influence future urban growth. Land zoned for urban development is determined by the State Government through the Western Australian Planning Commission with the availability of essential infrastructure being just one determinant of the urban potential of land. It is not the role of a water provider to influence the pattern of urban development, but rather this should occur as a combination of broader state government planning coupled with market drivers.

It is UDIA's unequivocal position that standard headworks charges across WA provide the development industry with certainty and reduced risk which translates to a more cost efficient product for the market. With declining affordability in WA a very real problem for particular sectors of the market, it would be irresponsible of the Water Corporation to introduce pricing mechanisms for water infrastructure that are likely to have a negative impact on housing affordability, particularly in regional areas.

3. Special developer contribution area charges

It is UDIA's view that the facility for the property industry to negotiate Special Contribution Area Charges if and when they occur should continue. As with all calculations, this process must be transparent to ensure that the outcome is fair and equitable both to the developer and the service provider.

A formal review process for Special Developer Contribution Area Charges should be established and undertaken on a regular basis to monitor the need for these charges. It is important to keep track of the relevance of the charge to determine when it is no longer required, so that the property industry and in turn the consumer are not overcharged. A case in point is the recent removal after more than 20 years of the Special Area Charge over the North West Corridor. The charge was not subject to regular review and was applied unnecessarily for many years. It could be argued that refunds to developers should be provided if over charging occurs. This outcome must be avoided in future application of these charges.

4. Cost recovery of minor works

UDIA fully supports the cost sharing of minor works between developers and the Water Corporation and believes that it is a fair and reasonable approach. The developers charged must be those with a direct benefit on the land impacted by the minor works.

As with any charges, these should be applied in a transparent manner, with all costs detailed and accounted for.

5. Major customer charges

UDIA makes no comment on this item as these charges apply primarily to the mining industry.

6. Headworks contributions for temporary connections

Appropriate charges for a temporary connection depend on the capacity of the local scheme to cope with extra demand in the short term. It is UDIA's view that charges for temporary connections should be established on a case by case basis, and reflect the location and projected demand that the connection will have on the scheme.

UDIA encourages consideration of the use of alternative water sources for temporary needs. It is concerning to the industry that potable water is still used for dust suppression. Temporary connections could be a significant way of decreasing reliance on scheme water and assistance from the Water Corporation in accessing these sources would be advantageous.

Additional comments

UDIA is of the opinion that this review should also consider the use of offsets for headworks charges. Offsets offer a form of competition that is appropriate to the water market and it is incumbent on regulators to incentivise and legitimise the use of offsets so that the appropriate use of all forms of water has greater traction in the industry. There is no place for water re-use in the form of treated wastewater or recycled grey water under current pricing structures, and the authority needs to reflect the innovative use of water in all its forms through pricing mechanisms which offer incentives to the development industry to promote alternative water uses. UDIA believes that developers should be encouraged and rewarded for thinking 'outside the square' when it comes to implementing the use of alternative water sources in their developments.

As an example the first 'third pipe' scheme in residential development in Perth paid full headworks charges for the potable scheme when only 50% of the water demand for 1500 dwellings will be required. At the same time the developer had to fully fund all headworks infrastructure for the non-potable scheme. There need to be offsets from potable to non-potable schemes as well as other financial incentives for developers to pursue water efficiencies and source substitution that are in the community's best interests.

Conclusion

UDIA strongly supports uniform headworks charges across Western Australia and we advocate for maintaining the status quo as far as developer contributions are concerned. We believe that the current system works well, it provides certainty to the industry and there is nothing to be gained from changing it. In a climate of decreasing affordability and increasing development costs, it is incumbent on the Water Corporation to provide infrastructure that facilitates proper and orderly planning so that industry can deliver new lots to the market in an efficient and timely manner.

Thank you for the opportunity to comment on the Inquiry's issues paper.

Yours sincerely

Debra Goostrey
CEO UDIA (WA)



ATTACHMENT 1

Letter to Mr. Stephen Hiller re bonding arrangements by Water Corporation

4th December 2007

Stephen Hiller
Manager
Development Services
Water Corporation
PO Box 100
Leederville 6902

Dear Stephen

The Urban Development Institute of Australia (UDIA) WA is the peak body for the land development industry in Western Australia and is represented on the UDAC sub-committee. The UDIA Infrastructure Committee met today and discussed changes to Water Corporation's bonding arrangements. There were two major concerns: firstly, the impact of these changes on the industry and the purchaser and secondly, insufficient industry consultation.

At the UDAC sub-committee meeting on the 30th August the issue of bonding was discussed and UDIA representatives agreed in principle that bonding should generally only be used for works which are already underway to achieve timely release of titles to enable land to be sold and for purchasers not to be disadvantaged.

Representatives expressed concerns about some of the detail of the Water Corporation proposal which was tabled at the UDAC meeting on the 19th September including:

- The actual proposed bond amounts
- What to do in the case of headworks which may be many months or years away, in areas which may not even be planned yet
- How to handle "penalties" when in many cases the delays may be due to Water Corporation or other factors outside the control of the developer

At the September UDAC meeting you provided assurances that the proposal was not yet finalised however there was no further consultation prior to Water Corporation issuing the letter and information sheet on the 19th October detailing the bond conditions. UDIA members are extremely concerned that this lack of consultation has resulted in a proposal that will have unexpected consequences and a disastrous impact on affordability in the longer term. The substantial penalty provisions could result in developers forfeiting up to \$40,000¹ per week of the bond for a standard subdivision. This is completely unacceptable to the industry and will be vigorously opposed as it will lead to an escalation of prices during a period of acute affordability pressures.

¹ This is based on a standard 50 lot stage at \$8,000 bond per lot giving a total of \$400,000 in bonds. In the policy the developer forfeits 10% of the bond amount for each calendar week that the take over date is delayed.

In relation to the impact to the industry and the purchaser there are two separate issues that need to be addressed. Defaulting has a clear impact on both the Water Corporation and the purchaser and industry supports strategies to ensure that developers who default are not given the benefit of future bonding.

The issue of delays on takeover dates has no discernible impact on Water Corporation with the exception of complaints management. The key issue appears to be the impact on consumers where movements in the completion date of water connection delays construction of their house resulting in holding costs² and potentially an escalation in building costs.

Bonding, when done appropriately, decreases costs by allowing titles to be issued and purchasers to commence their works at an earlier date which reduces holding costs for both parties. UDIA studies show that for each six month delay, for what ever reason, a cost of \$17,700³ is incurred on an average priced block⁴. Even small delays can add significant costs so bonding is an essential strategy in delivering affordable lots to the market. The forfeiting of 10% of the bond in accordance with the new policy would result in an \$800⁵ per lot per week penalty for the developer and this cost will be passed on either through contract clauses in the civil contract which will escalate prices or through an increase in lot pricing to cover the risk. This increase in lot price would negate the benefit of bonding. In some cases developers will regard the risk of bonding as too great and will no longer bond works. This will have a significant impact on purchasers.

Bonding assists the purchaser to move into their home sooner, saving on alternative accommodation costs. The bonding facility enables the clearance and title process to be advanced, and is usually timed such that titles can be obtained around completion of the subdivision works. Thus the lot purchaser's builder can have building plans approved by Council, be on site soon after the subdivision works are completed and construct the slab within a few weeks. Without bonding the purchaser would face extra rent plus eight weeks of price escalation in building costs. Industry estimates that the purchaser would face extra costs of around \$7,400⁶ if there was no bonding.

Developers too would face additional costs if there was no bonding and it needs to be understood that the developers will eventually pass additional costs through to the market. Given the government's concern about the affordability crisis impacting on this state it would seem counter productive to introduce measures that escalate the price of lots. Industry estimates that developer holding costs would be approximately \$3,200 for a first home buyer lot and \$5,300 for an average Perth lot. Of course these costs would have GST, and in some cases, Stamp Duty applied. The whole of life cost for the purchaser is significantly more when the interest paid over a standard twenty five year loan is taken into consideration.

Delays in the provision of headworks impact negatively on the developer who may need to pump waste or take other interim measures, which provides motivation for early completion. Delays in the delivery of bonded headworks should not have any financial impact on the Water Corporation or the purchaser. Bonding can work extremely effectively where either non-essential services

² Additional interest/rent etc

³ UDIA figures as provided to Dept Treasury and Finance August 2007

⁴ Based on UDIA's UDI data June quarter 2007

⁵ Based on an average bond of \$8,000 per lot

⁶ Rent @ \$300 per week = \$2,400 plus notional price rise in building costs is \$5,000.

are bonded, for example a pump station, where the provision of the service/infrastructure is not required at the point of building. It can also be used successfully for essential services when the construction of the service is near completion and the developer wishes to bond in order to move through the clearance procedure more rapidly as bonding avoids all of the time consuming inspections and checking of the works and plans until after the title has been issued.

Concern was also expressed by UDIA members that measurements which determined poor performance, which is stated as the motivation for the new Water Corporation proposal, were undertaken during one of the biggest property spikes in Perth history where the demand for land, and therefore the pressure applied on human and physical resources, was at its peak. Across industry sectors and government departments there were extensive delays that were caused by the state of the market and it is unreasonable to condemn the industry for their on-time performance during that period. It is also unclear as to how many purchasers actually incurred additional holding and construction costs through the delay. Industry feedback is that this figure would represent a tiny fraction of lots completed which brings into question why such a small percentage would trigger such a draconian policy response by Water Corporation.

The legality of Water Corporation implementing the forfeiture of a percentage of the bond as a penalty has also been questioned by the industry particularly in light of the recent determination by the NSW Independent Pricing and Regulatory Tribunal that a business entity could only charge penalties when both parties were compensated for delays caused by the other party.⁷

It is noted by the industry that realistic time lines for hand over should be provided by the developer to avoid negative impacts on purchasers. This change of behaviour does not require a strategy that could potentially add thousands of dollars to every lot through the necessary management of potential risk by the developer. What is required is better communication between industry and Water Corporation.

UDIA representatives would like the opportunity to discuss a process by which developers could apply for an extension to the hand over date, which would enable data collection on the major causes of delay and closer tracking by Water Corporation. As identified above, many of the delays are outside of the control of developers and this data would be exceptionally useful in tracking the causes. Sometimes it can be as simple as a delay in obtaining a dewatering license. Once the causes of delay are identified consultation with industry should then focus on addressing the causes. The data tracking would also enable the identification of recalcitrant developers who could be dealt with by Water Corporation under separate arrangements that do not punish the broader industry.

Representatives of UDIA would like to meet with you as a matter of urgency to discuss this issue and alternative pathways to reducing discrepancies between forecast and actual completion dates.

⁷ Finding by the NSW Independent Pricing and Regulatory Tribunal in reference to Patrick and P&O (now Toll and DP World) in relation to the vehicle booking system

Please contact me on 9321 1101 if you would like to discuss this matter further.

Yours sincerely

Debra Goostrey
Chief Executive Officer, UDIA (WA)

cc.
Dr Jim Gill Chief Executive Officer Water Corporation
The Hon John Kobelke Minister for Water Resources
Marion Thompson Land Release Coordinator DPI