Submission
No 168

INQUIRY INTO DEVELOPMENT OF THE TRANSPORT ORIENTED DEVELOPMENT PROGRAM

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Submission to the NSW Legislative Council Inquiry into the Transport Oriented Development Program

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Submission on the proposed low- and mid-rise housing policy

Introduction

I was previously the Professor of Urban Planning at the University of Sydney. I am now an Emeritus Professor at that same University as well as an Adjunct Professor of Urban Planning at Monash University as well as a part time consultant.

One of my roles at the University has been to teach urban planning students the economics of property. I also led the PLANED program for the Department of Planning in 2014 which provided a series of CPD workshops for practising planners across NSW aimed at increasing their property economics skills. I have also delivered training to a variety of Local Councils and through the NSW Planning Institute I have led a short course on Property Economics for Planners for a number of years. My aim in this work has been to help planners understand basic property economics. Looking at the proposed plans with low and mid rise housing I can see that my efforts have had very limited impacts on the Department.

Let me begin by saying that I completely support the aim of increasing the amount of missing middle housing stock in Sydney ie some more low and medium rise stock ranging from terraces to mid-rise apartment blocks. However, the approach outlined in Department of Planning's Explanation of Intended Effect will not deliver the intended outcomes. In many cases it will restrict the ability of the Six Cities to deliver more density in future years. It will have the effect of making large tracts of housing in Sydney more expensive.

Why are dwelling supply levels so low at the moment?

It is clear that current levels of dwelling approvals and completions are down substantially on averages over the last 10 years. The public discourse seems to suggest that the only reason for this is local councils and particularly NIMBYs. However, what we are experiencing is a normal cyclical downturn resulting from the sharp increase in construction costs as well as the significant increase in interest rates. With the increasing focus of the Sydney markets on apartments, the ability to turn dwelling approvals into completion depends on being able to gain access to construction finance. The nature of apartment blocks makes them a much higher risk lending category because the financier has to fund the entire building before any revenue is received by the developer (unlike greenfield subdivision which can be built in smaller stages). Over recent years, the commercial banks who are the major source of apartment funding in Australia have attempted to contain their risks by instituting tighter lending criteria. They have reduced the loan to valuation ratios for projects forcing developers to use their own equity or more expensive mezzanine finance[1] to enable projects to commence. They have also increased the levels of pre-sales required on projects to around 100%. For some developers this level of presales has been very difficult to achieve exposing their project to substantial increases in construction costs further undermining their ability to demonstrate a sufficient level of profitability to access construction finance (even if they could meet the other conditions from the bank). You can clearly see this issue by comparing the recent levels of apartment approvals in Sydney with construction data (commencements and completions) or by examining the number of apartment approvals in

[1] Mezzanine finance is usually 7-10% more expensive than bank finance

2022 that have not yet received a construction certificate (from the NSW Planning portal). The level of pre-sales is also being hindered by the lack of public confidence in construction quality after the problems with Mascot Towers and other recent Sydney apartment projects. Ironically, providing more apartment approvals in Sydney is likely to make the situation worse in the short term because more developers will be competing in the same market to reach their pre-sales target.

Issues with the proposals

I have seven main problems with the current proposals:

1. Manor houses
2. It makes no sense from a property economics perspective to have the same rules applying across the 6 Cities when the housing markets are so different
3. The rules as proposed will sterilise opportunities for higher density in the medium and long term in Sydney (say the next 50 years)
4. It will undermine effective collaboration between State and Local Government planning because it fails to distinguish between Local Governments who have attempted to build high quality higher density communities and those that have frustrated State Government housing targets
5. It has the potential to undermine public confidence in the planning system
6. It is giving uplift away to property owners for free – it should be charging for Affordable Housing
7. It will make large tracts of Sydney's housing more expensive.

1. Manor Houses

I don't know what it is about Manor Houses (small two storey apartment blocks)– they have appeared in the previous complying development code but Sydney has built a tiny amount of them. Whilst people have accused councils working against their introduction, it is easy to see why they aren't being built in Sydney.

Table 1 below shows the amount that developers over recent years have been paying for apartment sites in Sydney. Four cases are selected showing central, inner, middle and outer Sydney. It makes no business sense for a developer to build manor house apartments when they are competing with apartments who will usually be better located, likely to have better views, the advantages of a lift for older purchasers, unless they can provide them at a better price point. However, manor houses will be substantially more expensive than traditional apartments because of the differences in land cost as shown in Table 1.

I have put this example first, not because I think it is the biggest issue, but because it is the best example of the current proposals ignoring basic property economics.

2. It makes no sense from a property economics perspective to have the same rules applying across the 6 Cities when the housing markets are so different

Just a cursory look at Table 1 shows the vast differences in housing markets across Sydney. Looking at the Six Cities the differences are even greater. Expecting the same sets of rules to apply in terms of heights and FSR makes little sense. As land values rise you need taller building to offset the costs of more expensive lands which is the reason that taller apartments buildings are seen in more expensive areas. Looking across the Six cities there will be some areas where six storey apartment buildings won't be built because there is no market for them because of their price points (an apartment price is too close to the price of townhouse with a small backyard to make it attractive for prospective purchasers). The harm of overzoning neighbourhoods with the one set of rules is that landowners get an inflated sense of the value of their property (they look at sales of 6 storey apartment land which is nearest to their lot) which often means they won't release it to the market for a less intensive land use (like townhouses). There is no better example of overzoning than the Department's previous City Centre Plans in 2008 when six commercial centres[2] in the Six Cities region were upzoned. For example, Penrith was upzoned to 25 storey commercial building which increased price expectations of landowners and reduced rather than accelerated market activity.

3. The rules as proposed will sterilise opportunities for higher density in the medium and long term in Sydney

This problem is related to issue number 2. Whilst six storey apartments make sense in some parts of the Six Cities Region, they are not high enough for many areas around train stations and major centres. If you are thinking long term you need to preserve those places for much taller buildings. Once you build a six storey building you lose the opportunity for a much higher density later. Looking at land values we can see why this is the case. Let us assume we convert a residential lot near a light rail station in the Inner West LGA to a 6 storey apartment block. Let us further assume (see Issue 6) that a developer pays the property owner $6 m for the site. If another developer wanted to replace that 6 storey building with a taller building they have to buy out say 30 apartment owners (5 per floor). If each of the apartment owners wanted a 25% price premium that would cost you (in today's prices) about $33 million dollars[3]. You would also have the additional problem of having to convince at least 75% of the thirty owners to sell. This price is so high it would make the development not viable. **The mistake people make is that they are outraged when they see detached housing near a Sydney train or light rail station. However, that detached housing provides an efficient land bank for future high density housing opportunities for the growth of Sydney overt the next 100 years.** Once you decide on a density (like the current proposals), you are stuck with that for a long time.[4] This is well demonstrated in Burwood where two storey apartment buildings sit next to much larger towers despite having similar zoning rules (see Figure 1).

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[2] Parramatta, Liverpool, Penrith, Gosford, Newcastle, Wollongong

[3] Looking at table 1 if you were considering a 12 storey apartment block, the apartment land cost would become 550,000 per apartment much higher than the current market values shown in the table.

[4] Except in very high value areas such as near Sydney Harbour where apartment selling costs enable developers to buy out smaller apartment buildings.

Table 1. Why Manor houses don't work

LGA	Address	Sale Price of Land Parcel (1)	No of apartmnts (2)	Land price per Apartment (1)/(2)	Median House Prices[a]	Median apartment Price [a]	Land price per apartment Manor Houses [b]
Penrith	Lethbridge St Penrith	$3,050,000	58	$52,586	0.895	0.575m	$223,750
Cumberland	Essington St Wentworthville	$1,720,000	21	$81,905	1.180m	0.560m	$ 295,000
Inner West	Hill St, Dulwich Hill	19,800,000	71	$278,873	2.040 m	0.875m	$510,000
North Sydney	Walker St North Sydney	$98,305,199	189	$520,133	3.375m	1.2m	$ 843,750

a. Rent and Sales Report data for LGA June quarter 2023.
b. Assuming 4 apartments per Manor House

Source: Search of recent development sites on stashproperty.com.au

The same issue relates to low rise housing. You want to protect land near stations and major centres in Sydney at least from low rise housing. Putting low rise housing within 400 sq metres of a train station makes it much harder for a developer to later purchase the land for an apartment building because of both the increased costs associated with the higher density as well as the difficulty of convincing enough strata owners to sell. Whilst some low rise housing could work well in an integrated development with a series of apartments within 400 metres of a train station, you would need to make sure that key apartment sites within 400 metres aren't sterilised for future opportunities by allowing them to be used for low rise housing. This sort of detailed planning cannot be achieved by a one size fits all approach and requires some careful local level planning.

4. **It will undermine effective collaboration between State and Local Government planning because it fails to distinguish between Local Governments who have attempted to build high quality higher density communities and those that have frustrated State Government efforts**

Looking at the performance of Local Councils in Sydney in relation to higher density it is clear that some councils are performing much better than others. For example, the City of Sydney has delivered some excellent high density precincts such as Green Square. Asking them to use the same rules as low performing councils does not acknowledge these differences in performance. Another Council is Hornsby who used a community deliberation process to focus their development in the Hornsby town centre and have advocated for very high residential densities rather than spreading apartments across their LGA.

Treating all councils as incapable of providing their own planning schemes to achieve low and medium rise development will generate resentment across these well performing councils and break down the levels of collaboration needed for run a successful planning system in a Global City. In my list of suggestions, I describe a system where different approaches are adopted for different Councils.

5. **It has the potential to undermine public confidence in the planning system**

It is difficult to argue with the logic of having apartment building within proximity of a train station or a light rail stop or a major centre with good transport connections. However, there are many centres with E1 and E2 zoned land with very poor public connections that suffer from poor accessibility especially in peak hours. I think a more sophisticated approach to selecting the centres other than the approach indicated in the proposal needs to be considered. Putting 6 storey apartments in all E1 and some E2 centres will not generate the benefits from locating apartments in areas with high transport accessibility. Spreading 6 storey apartments across a larger number of locations also runs the risk of alienating the public support for the planning changes. This will be exacerbated by the poor urban design outcomes from the low rise housing component, a point which is well argued in the submission by the Australian Institute of Architects.

6. **It is giving uplift away for free – it should be charging for Affordable housing**

Upzoning works by making land more valuable. At the moment the lucky land owners within 800 metres of the designated centres are given a windfall. Let's take someone in the Inner West located near a light rail station. If they have a large lot they have the potential to sell their land for up to about 280k per apartment (Table 1). Let's say they are not great at negotiations and they sell their site for $200,000 per apartment site. If we assume the yield of 30 apartments the sale price is $6 million, almost three times the current median price. Why should they receive the windfall without making a contribution to an affordable housing scheme. The current proposal says the Government will get to this issue later – but if you do that you are losing opportunities to collect revenue for Affordable Housing. Moreover, the current approach to delivering Local Council Affordable Housing Contribution Schemes is to charge based on rezonings. Once the State Government undertakes this large scale rezoning this opportunity will be gone.

7. **It will make large tracts of housing more expensive**

As discussed above and described in Council submissions, this policy will effect the majority of housing lots in some Councils, particularly those in the inner and parts of the middle ring. This means that for households trying to purchase a detached house in these suburbs (the upsizers) they will now be competing with developers. Existing homeowners are now more likely to hold out for a windfall gain from selling their property to a developer rather than to an upsizer. This will be good for apartment supply and hence apartment prices but put upward pressure on the prices of detached houses. You could get the same response in the apartment market and not put so much pressure on the prices of detached housing by limiting the upzoning to strategic locations where the viability of apartment buildings is certain.

Suggestions

1. Exclude manor houses from the proposal. Manor Houses have generated a lot of heat for potentially very little in the way of housing outcomes;
2. Remove the reference to apartments in LGAs in the 6 cities where apartments are not viable (mostly outside Sydney) in order to not inflate price expectations
3. Remove the non refusal conditions for low rise housing within 400 metres of train stations where apartments are currently viable
4. Consider limiting 6 storey opportunities around centres that are likely to need higher densities within the next 25 years
5. Provide realistic feasible housing estimates for each LGA using the current State wide proposals.

6. Do not adopt the plan in Council areas where the Council can demonstrate their current LEP will deliver more feasible housing opportunities than the current State wide proposals.
7. Consider a system where Councils with a good track record in low and mid rise development are given time develop a strategic plan to amend their LEP to generate more feasible housing opportunities than available in the current State Government proposals. If such a plan is forthcoming, the Council can also be exempted from the scheme
8. Introduce the State wide planning scheme in low performing LGAs (with the possibility of amending it in certain parts of their LGA – see suggestion 10.)
9. Establish a planning panel to help adjudicate which councils in each of the above three categories and to validate estimates of feasible housing opportunities..
10. Use this same panel to hear applications from Councils to exclude parts of their Council areas from the State scheme. This was a process followed in the case of the national upzoning of Auckland.[5] Having a blanket scheme without considering local circumstances is not really planning – it's just busy work. For example, in their draft submission the City of Sydney makes the obvious point that 6 storey apartments might not work in some parts of their LGA with very narrow streets. In the NZ system this would be considered a qualifying matter.
11. Limit the number of E1 and E2 centres impacted by the scheme based on their transport connectivity.
12. Develop a strategy to accelerate dual occupancies.
    The new dual occupancy rules are likely to achieve a significant response in the short term. This might be accelerated if the Department in collaboration with Councils conducted an information campaign that might help connect property owners in the same areas (eg within a couple of blocks). These property owning groups could then explore issues such as using their scale to provide more efficient contracting with built environment professionals and builders. They could be introduced as soon as practical.

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[5] **Auckland – the qualifying matters**

Some areas can be exempt from the six and three-storey requirements and the new design standards based on qualifying matters.

These are characteristics within some areas that allow for intensification to be limited, such as protecting sites of cultural, historic, or ecological significance or avoiding development in areas with natural hazards or where there are certain infrastructure constraints. However, a qualifying matter can only apply if there is strong evidence provided to justify an exemption.

The new medium density residential standards will not apply to properties with a proposed qualifying matter until final decisions are made in 2024 at the conclusion of the decision-making process. At that point, a proposed qualifying matter could be confirmed, removed or adjusted.

https://ourauckland.aucklandcouncil.govt.nz/news/2022/08/auckland-s-changing-planning-rules-what-you-need-to-know/

Figure 1. Site in Railway Parade Burwood with different built forms