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SUBMISSION ON THE LTCCP DEVELOPMENT CONTRIBUTIONS POLICY

To the Christchurch City Council,

Introduction

This submission is from Christian Jordan.

I work in the property industry and make this submission based on my personal observations. I made a submission to Council on the previous Development Contribution Policy in 2007.

If possible I would like to present my submission to council in person.

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Submission

Overview

The Development Contribution Policy (DCP) transfers the burden of infrastructure funding to the future owners of smaller, low value homes.

The affordable starter homes and the smaller centralised housing that our city needs, are being squeezed out by what equates to an excise on sensible, affordable and sustainable development.

If the DCP remains unchanged our city will not be able to provide the quality accommodation that first home buyers and tenants require. This will severely impact on the future of sustainability of the city of Christchurch.

Fairness

In New Zealand we accept that taxes based on a person's ability to pay is a fair and equitable way to distribute the tax demands amongst the entire population. Likewise rates demands are distributed so those who can afford to pay more take a larger share of the burden irrespective of the demand they create on resources.

For example: A \$200,000 house, home to a family of five pays only \$1000 in rates while a couple in a \$1,000,000 home pays \$4,000. That is \$200 per person per year in the cheaper house versus \$2,000 in the expensive house – our society deems this fair as it is.

Consider the DCP. A \$250,000 house to be built in Woolston for a young couple will need to pay \$30,000 development contribution. A \$600,000 house for a family of five in Harewood will pay \$22,000 and a \$1.5m home for a family in Fendalton will pay \$21,000. This will add just 1.4% to the cost of the Fendalton home, 3.7% to the Harewood home and will increase the cost of the Woolston home by 12.0%.

This means that owners of the least expensive new homes will pay Development Contributions at *ten times* the rate of the wealthy. This is the exact opposite of what our society general considers to be fair.

The young couple in the Woolston home will need to pay an extra \$50pw on a 25-year mortgage to cover the extra \$30,000. This will cost them an extra \$65,000 (in today's dollar terms), or if they had put the extra money into a savings scheme with a 3% real return this would be worth \$96,000 in today's terms.

The irony is under the old pre 2007 scheme (7.5% reserve contribution), the Fendalton house would have paid \$60,000 and the Woolston house \$7,000. So the poorest homeowners get a 430% increase whereas the wealthiest get a 67% decrease.

Impact

The full impact of the DCP has not yet been felt as the 2007 – 09 changes have only been slowly introduced. Once the flat fee scheme is fully implemented the sharp decline in building activity seen in the last year will be exacerbated by a complete collapse in the construction of affordable, smaller homes except on sites that already were consented prior to the changes.

This is Christchurch's very own Smoot-Hawley legislation. It may not be a tariff, but it certainly is an excise on affordable housing.

This will have long reaching consequences for Christchurch. In the short term less construction will occur. This is because during the current recession demand for large expensive homes (which are incentivised by the DCP) is low, while on the other hand lower house prices and increased building costs together with a 400%+ increase in Development Contributions on cheaper homes will make their construction in most cases totally unviable.

So with fewer homes constructed the economy suffers. Short-term, house and land prices fall further, making construction even less viable. Medium-term, supply of affordable homes dwindles forcing rents higher, which eventually turns house prices around. Ultimately, the market will price in the DCP so the price of all cheaper homes (including existing ones) will have risen relative to their larger more expensive counterparts.

Long-term redevelopment in the lower income areas of southeast Christchurch will grind to a halt; as punitively high stormwater charges will divert what little development that does occur in cheaper suburbs to areas of the city where the charges are lower.

Possible Future Outcomes

If the DCP is left in place, five years from now the Council will realise how the DCP has distorted the market. Such large increases in Development Contributions could easily be lost in the euphoria of a housing bubble, but in a moribund post Global Financial Crisis environment the distortion will become patently obvious.

A future Council will then likely change the policy to reduce the impact on affordable housing. The effect of this will be another market distortion – removing a cost that by that time will be priced into the market, will cause a flood of lower priced development, as up to an additional 10% profit margin would have been created.

If the housing market is still flat (which is likely given the size of the recent boom/bust cycle and the structural macroeconomic changes that have and will take place) then the removal of the DCP in five years time will likely drive the price of affordable housing down below where it had been.

Having distorted the market upwards with the proposed DCP it's inevitable retraction will distort the market back down.

This will leave those future buyers of lower-priced homes (who as predominantly first time buyers or investors are highly leveraged) in negative equity positions, causing economic pain to the city. As a worst-case scenario, in a possibly still weak global and national economic environment, this could lead to a localised depression of the type that Southland and Otago experienced from the 1970's through to 2000.

Alternative Impact

There may be a tendency to believe that increasing Development Contributions will only impact on the developer and the price paid for undeveloped land.

Consider this example. Today an average subdivided rear section (300-450m² depending on zoning) in an average lower-middle income part of east Christchurch will retail at just under \$100,000. An average older house on a subdivisible full section in this type of area sells at around \$275,000. An average older house on a subdivided section in this type of area sells at around \$215,000.

To subdivide the section, all professional fees, consent fees, services, driveways and fencing etc will cost a minimum of \$20,000, normally \$25,000. Add a further \$30,000 in development contributions, then this gives a net value of the undeveloped land of just \$45,000 before considering a developer's margin.

However subdividing the property will reduce the existing houses value by \$60,000 so the development is totally unviable. If this property was developed the owner would **lose \$15,000** and that doesn't even consider additional sale or holding costs.

With the section prices falling by nearly 30% from their 2007 peak and fixed costs rising, the margin for subdividing has virtually evaporated. The final straw is increased DCP charges make developing low end sections totally unviable. The result is that new houses won't get built. That's bad for jobs, bad for Council revenue, bad for first time buyers and bad for the city.

A realistic DCP charge of no more than 10% of the land would return some viability to this type of development occurring. Even though the profit on subdividing would be small, the developer could make a margin on the construction cost of the house.

In this scenario construction would occur, jobs would be created, Council would have an additional revenue stream (rates from the new property of \$1300PA (equivalent to having \$10,000 capital), plus at least \$5,000 in consent fees, plus a \$10,000 Development Contribution – that's a total worth \$25,000 to Council that they wouldn't be getting with the proposed DCP), a first time buyer would be getting an affordable brand new home and the city will continue to grow and attract new migrants with relatively affordable housing.

The proposed DCP makes no economic sense. Developers will only develop if there is a margin, so until house prices rise (which they will if there is no supply) this type of development won't occur.

Please note:

As a property investor with interests in \$12m of residential property including over 1ha of L3 and L4 land in Christchurch, most of which is already fully developed or has consents under previous DCP, I would personally stand to see more benefit from seeing the new DCP implemented, however I strongly believe that the DCP's implementation would be of great detriment to Christchurch and greater New Zealand's economy therefore I am vehemently opposing it.

As an aside

With the average age of a house in Christchurch being about 45 years, the rates on a home worth \$250,000 today being about \$1200PA, and the growth in the cost of rates slightly above inflation then in actual nominal dollar terms the Council has collected just \$22,000 in rates on that average age \$250,000 house since it was built. This is \$43,500 in today's dollar terms.

As a back of the envelope calculation, if about 30% of rates goes towards capital spending then the average age \$250,000 house in Christchurch has only contributed \$13,000 towards capital expenses which it has had 45 years use of.

Yet the new neighbour is expected to pay up to \$30,000 for the right to use these assets when rates had already been paid on the vacant site since the inception of rates demands. (In the case of a subdivided rear section - perhaps \$300 per year of the current rates for the existing house is due to the additional value of the rear yard. Therefore, in today's dollar terms, over \$3000 that has been paid via rates towards capital contributions over the previous 45 years. So the existing \$250,000 house has only contributed \$10,000 more than the new one!)

To any rational thinking person this Development Contributions Policy does not display the level of fairness or equitability that New Zealanders would expect.

Solution

Charge no more than 10% of the land value or 4% of the total building cost in total development contributions.

Or:

For residential buildings charge a rate per square metre. This will remove the incentive to build larger homes, and will encourage smaller, sustainable and efficient housing.

To further incentivise affordable housing, a lower DC rate could be charged for housing that achieved certain social objectives. For example, stand alone homes of total floor area under 150m² in certain suburbs with finished market value under say \$330,000 might qualify for a DC rebate.

To guarantee a similar level of revenue for Council, the cap on total Development Contributions could be raised to say around \$45,000 provided pro rata maxima were introduced.

This is possibly the last chance that Council has to retract this disastrous policy before any more significant damage is done to Christchurch's economy.

I thank you for your time.