Master Builders Australia

Submission in response

to the

Inquiry into the Australian Government's Role in the Development of Cities

31 July 2017

CONTENTS

1 Introduction

1.1 Master Builders Australia (Master Builders) is the nation's peak building and construction industry association, and was federated on a national basis in 1890. Master Builders Australia's members are the Master Builder state and territory Associations. Over the past 125 years the movement has grown to over 33,000 businesses nationwide, including the top 100 construction companies. Master Builders is the only industry association that represents all three – residential, commercial and engineering construction sectors.

1.2 The building and construction industry is an extremely important part of, and contributor to, the Australian economy and community. It is the second largest industry in Australia, accounting for 8.1 per cent of gross domestic product, and around 9 per cent of employment in Australia. The cumulative building and construction task over the next decade will require work done to the value of $2.6 trillion and for the number of people employed in the industry to rise by 300,000 to 1.3 million.

1.3 With Australia's population expected to double by 2075, the building and construction industry will play an increasingly prominent role in providing the additional capital infrastructure needed to support the future development of Australian cities.

1.4 But there is evidence that regulatory barriers and red tape have, in the past, prevented the efficient construction of new capital infrastructure. For example, restrictive land release policies on the city fringes in Sydney have limited the construction of new housing and helped to push up house prices.

2 Background

2.1 We note the broad terms of reference of the current invitation of submission and the two distinct streams of inquiry. Given our existing body of research into the building and construction sectors of existing cities, including an assessment of the impact of reforms supported under a number of spending commitments in the 2017 Federal Budget, our submission will focus on the terms of reference of the first stream of inquiry into *sustainability transitions in existing cities (Inquiry 1).*

2.2 In terms of the three discrete items under the terms of reference for Inquiry 1, we note:

2.2.1 To *identify how the trajectories of existing cities can be directed towards a more sustainable urban form that enhances urban liveability and quality of life and reduces energy, water and resources consumption* – an examination of the benefits of better transport links and a more efficient housing sector, for households, will be determined under different policy reform scenarios in the household sector

2.2.2 *Consideration of what regulation and barriers exist that the Commonwealth could influence, and opportunities to cut red tape,* a detailed industry consultation of building business was undertaken, and included representatives from every major housing market in Australia. These consultations provide a list of priority areas of reform in the housing construction sector across all states/territories in Australia, and

2.2.3 *Examining the national benefits of being a global 'best practise' leader in sustainable urban development*, is considered to be a largely philosophical question and therefore better answered by more philosophically aligned organisations/institutions.

2.3 Within this line of inquiry we will focus primarily on a detailed examination of the regulatory barriers which can (1) be influenced by reform, or support of reform (incentive payments) at a Federal level, and (2) regulatory impediments identified by building businesses as the most binding in their respective state/territory building and construction sectors.

3 Purpose of this Submission

3.1 Master Builders is pleased to have the opportunity to provide a submission to the Inquiry into the Australian Government's role in the Development of Cities, with the following sections of this submission to build on recommendations outlined in our 2017 Pre-Budget submission.

3.2 The primary purpose of this submission is to provide support for reforms in the housing and infrastructure construction sectors, with the aim of reducing pressure on housing affordability and filling Australia's infrastructure shortfall.

3.3 It is hoped that the findings of this research (contained in this submission and in the attached supporting documentation) provides a platform for funding to be allocated under measures such as the $1 billion Housing Infrastructure package and the $375 Affordable Housing and Homelessness package outlined in the 2017 Federal Budget.

3.4 In short, cities must, as a first priority, be sustainable for the people who live in them. Delivering better housing and transport infrastructure is a critical first step in making our cities more affordable (and therefore more equitable), increasing the living standards of residents and reducing the future costs of housing and transport.

4 Overview

4.1 Cities are the engine of growth in any developed country economy. Indeed, a recent McKinsey report mapping the global economic power of cities estimated that 60 per cent of global GDP comes from the top 600 world cities – with all of Australia's major state capitals amongst them.

4.2 *The World Urbanisation Prospects* (2014) report, published by the UN Population Division, showed Australia is amongst the most urbanised populations in the world with more than 90 per cent of our population choosing to live in an urban environment[1]. Therefore, development policy which harnesses the economic power of cities is more important in Australia than in most countries.

4.3 But as noted in a recent report by the International Monetary Fund, not only is our population "highly urbanised"…"but the very large population share of our two major cities sets us apart from most other highly urbanised advanced economies." About 40 per cent of Australia's population is captured within the city limits of Sydney and Melbourne.

4.4 This combination of high urbanisation rates and low city density has a significant impact on house prices, and therefore living costs, in Australia. Australia's two city structure imposes population pressure on these dominant urban hubs, creating scarcity and pushing up the price of well-located land.

[1] Urbanisation rates in comparable countries such as Canada, the UK and the US all hover around 85%.

4.5 The impact of our highly urbanised but low density city structures was examined in a Reserve Bank report; *City Sizes, Housing Costs, and Wealth* (2001). The report found "that dwelling prices tend to be higher in large cities than in small ones. Therefore, the expensive cities in Australia drag up the average level of dwelling prices more than in other countries."

4.6 In doing so the paper finds that the spatial aspects of demography are important for the level of non-financial wealth and house prices, in much the same way as demographic factors of the labour market and population.

4.7 The impact of planning and zoning policy for cities, and particularly in the housing sector, has featured in a number of Government reports, including from the Productivity Commission[2] and Treasury[3].

4.8 Planning and zoning reform was also featured in the recommendations of the Henry Review, noting:

4.8.1 **Recommendation 69:** COAG should place priority on a review of institutional arrangements (including administration) to ensure zoning and planning do not unnecessarily inhibit housing supply and housing affordability

4.9 But perhaps the most compelling case in support of better city development policy comes from research by Robert Shiller, the co-creator of the Case-Shiller Home Price Index and 2013 Nobel Laureate, in a recent piece of work examining the social implications of the wealth effects of high house prices in big cities.

4.10 The research finds barriers to housing construction as the predominant reason for high house prices, but more importantly it also finds that once a city runs out of available building sites (or these available sites are restricted through regulation) its continued growth must be accommodated by the departure of low income people.

4.11 In doing so the end point of this trend is that house prices become a social chasm in which the incumbents (known as NIMBY's in the local context) resist further construction as a kind of rent seeking by homeowners looking to protect the price of

[2] Productivity Commission 2004, First Home Ownership, Report no. 28, Melbourne

[3] Council of Federal Financial Relations 2016, Affordable Housing Work Group: Issues Paper, The Treasury, Parkes ACT, 2600.

their asset. This in turn creates inequality, with the expensive city becoming an enclave of high-income households, and begins to take on their values. Or as Shiller puts it:

"A city with a high housing-price-to-income ratio (high house prices) is less a 'great city' than a supply constrained one lacking in empathy, humanitarian impulse, and increasingly, diversity." (R. Shiller 2017, Project Syndicate)

4.12 Master Builders also acknowledges the National Cities Performance Framework (Interim report), published recently by the Department of Prime Minister and Cabinet. Following on from a range of measures targeting housing affordability and infrastructure investment, Master Builders welcomes the intention to create a performance framework to assess Australian cities across a range of metrics.

4.13 With Australia population expected to reach 30 million by 2030[4] the demand on our cities resources, infrastructure and housing markets is going to become even more acute over time. Our cities and the people (human capital) in them is Australia's most valuable resource. Investment into improving the productive capacity of our cities is an imperative if we are to improve the living standards of all Australians and provide a productive platform for business to grow and prosper.

5 Master Builders Australia Response

5.1 As part of our Pre-Budget submission Master Builders expressed a number of concerns in this area and outlined a role for the Commonwealth Government to play in supporting a more efficient agenda for capital investment and development in our major cities.

5.2 Subsequent research, which has been used to inform the analysis in this submission was undertaken to show the potential economic benefits of reforms targeted at the housing and infrastructure sectors in terms of their economic and social contributions[5].

[4] Using population project Series B from the Australian Bureau of Statistics, Population projections, Australia, 2012 (base) to 2101. Cat no. 3222.0

[5] Please find a copy of Master Builders Australia Pre-Budget Submission in Appendix A

5.3 There is a consensus across governments and in the private sector that better transport infrastructure is need to improve the productive capacity of cities in Australia. Infrastructure Australia estimates Australia's infrastructure shortfall at approximately $700 billion.

5.4 The housing market has also been in shortage for a number of years. Dwelling investment fell from its relatively consistent long run average of 6 per cent of GDP, to average 5.5 per cent over the decade starting in 2004. This may not seem like much but over a decade, this added up to a shortfall of over $83 billion, enough to build an extra 165,000 new homes.

5.5 The industry has been playing catch-up in the last two years, with new housing completions outpacing population growth over this period. But by the Governments own estimates the housing sector is still falling short of demand by around 100,000 dwellings.

5.6 With the supply of infrastructure and housing in Australia's major cities not keeping pace with demand, city residents (60 per cent of Australia's population) are challenged by longer commute times, higher living costs, and lower household consumption as more resources are allocated to less efficient housing and transport. This in turn reduces disposable incomes and lowers the living standards of city residents.

5.7 Restoring balance in these markets is therefore a critical element in ensuring the sustainability of existing cities in Australia, and may provide significant benefits to households by reducing the cost of living and improving the quality of life of residents.

5.8 We know that a shortage of shovel ready land, combined with embedded regulatory and tax costs can amount to 30-40 per cent of the cost of a new home – putting a floor under house prices and sucking up extra capital which would otherwise be allocated to building more new housing.

5.9 A report by Cadence Economics, commissioned by Master Builders, examined the Federal Government's transport infrastructure spending measures funded in the Budget in terms of the potential impact on living standards and the housing sector in Australia. At its centre is a $75 billion transport infrastructure package, complemented by an additional $1 billion to address infrastructure bottlenecks in residential development areas.

"Nothing increases the supply of well-located land like good transport links." (Phillip Lowe, RBA Governor, 2017).

5.10 Transport investment funding in the Budget forward estimates is forecast to support the construction of up to 93,000 additional new homes by 2021, boosting supply by 41 per cent.

5.11 This funding is also slated to support an additional $5.6 billion in revenue in the building and construction sector and create an additional 4,200 permanent building and construction jobs each year over the next five years.

5.12 Households are expected to be the biggest beneficiaries, $3.2 billion better off, measured in terms of household consumption, as more people have the opportunity to own their home, and transport infrastructure links are made more efficient.

"Correctly targeted 'city shaping' transport infrastructure can effectively boost the supply of housing land… Such expansion in effective land supply for housing can place downward pressure on house prices." (National Housing Supply Council, 2013)

5.13 However, in order to provide this extra infrastructure and housing in a timely and efficient manner, regulatory impediments which block the efficient delivery of major infrastructure projects and new housing must be removed.

5.14 To identify which areas of regulation are the highest priority of reform - or put another way, this regulations which are the biggest barriers to the construction of more new housing - Master Builder undertook detailed and comprehensive consultations with building and construction businesses across the country. Respondents were wide ranging and representative of all major housing construction markets in Australia, as well as a number of building services and supplier businesses.

5.15 Consultations focussed on supply-side issues, and specifically on issues which can be addressed through the implementation of a financial incentives agreement between the Commonwealth and state/territory governments.

5.16 A number of challenges, such as rising developer/infrastructure charges, were a consistent theme across most jurisdictions, while other issues, such as the cost of compliance during the build phase of a new housing development were found to be more pressing in some jurisdictions than in others.

5.17 A number of issues were raised consistently across housing markets in Australia, including:

5.17.1 **Inadequate land supply** – this is a result of land release which is either too slow or not adequate to satisfy demand in locations where people want to live – often as a result of long lead times in planning and development or from delays during this process. This was identified either as a top or high priority in each of the states and territories.

5.17.2 **Embedded land costs** – this encompasses regulatory charges, approval waiting periods, compliance cost and headworks fees, and was nearly uniformly identified as a top priority issue (if not the top priority issues);

5.17.3 **Infrastructure and developer charges –** this was again nearly uniformly identified as a top priority issue, with the exception of Queensland and South Australia where it was identified as a high priority issue.

5.17.4 **Poor planning and zoning** – were identified in New South Wales, Victoria, Queensland, Western Australia and the Northern Territory as top priority impediments to the construction of more new homes.

5.18 A number of other issues were raised as top or high priorities in some States/Territories but not in others. These include:

5.18.1 **Red and green tape** – this is a broad category which included waiting periods and administrative costs associated with development approvals, building and design approvals, environmental assessments, mitigation costs and expert reporting. New South Wales, Victoria, Tasmania and the Norther Territory all identified growing red and green tape as a top priority;

5.18.2 **Compliance costs –** this includes costs accrued during the build phase for compliance such as the cost of certification of design and construction, compliance to the National Construction Code and meeting energy efficiency standards. Tasmania and the Northern Territory identified this as a top priority; and

5.18.3 **Inflexible planning schemes –** a number of residential builders noted a lack of flexibility when planning schemes do exist. Planning documents often create rigidity in the allocation of land for different purposes. These documents often have a long outlook, which is needed to provide long term certainly for investors and developers, but the demand for land can change more quickly and planning regimes which do not allow for flexibility can cause land to be allocated inefficiently. The Northern Territory identified inflexible planning schemes as a top priority, while New South Wales, Victoria and Tasmania also all identified this as a high priority for reform.

5.19 A full list of all the issues raised during the consultation process can be found in the attached documentation to this submission.

5.20 Whilst the consultation process identified a number of consistent issues facing housing markets across Australia, it also highlighted a number of different challenges, and perhaps more importantly, the need for Federal Government policy to be flexible and able to be tailored to best target the areas of highest priority across the different housing markets in Australia.

5.21 Feedback from this consultation process was used to inform further research into the impact of reforming these priority issues. A modelling framework, informed by the Reserve Bank of Australis's discussion paper *Urban Structure and House Prices: Some Evidence from Australian Cities*, and the Computable General Equilibrium Modelling framework of Cadence Economics.

5.22 The following section provides a summary of the key findings of this analysis and what can then be drawn from in the formation of better cities development policy.

6 Impact Analysis - Policy Scenarios

6.1 Constraints in the supply side of housing markets have been identified through a number of key public sector inquiries including by the Productivity Commission and the Federal Treasury as a key contributor to sustained high house prices and rents. With these lessons in mind, this section tests the housing market and demonstrates the potential macroeconomic benefits of better housing supply and city structure policies.

6.2 In the Reserve Bank of Australia research discussion paper *Urban Structure and Housing Prices: Some Evidence from Australian Cities*" (Kulish, Richards and Gillitzer, RDP 2011-03) the impacts of supply side reforms on a stylised major Australian city are demonstrated.

6.3 To build on this work, a recent report by Cadence Economics, commissioned by Master Builders, provides an examination of potential areas of reform under different policy scenarios, by:

6.3.1 adjusting the housing market model for representative small, medium and large Australian cities, allowing for differential impacts by city size;

6.3.2 using the distribution of city sizes across the states and territories to estimate aggregate impacts by state and territories, and

6.3.3 using a Computable General Equilibrium model to assess the broader economic consequences.

6.4 The three scenarios of reform modelled as part of the examination, include:

6.4.1 Developer charges and planning delays

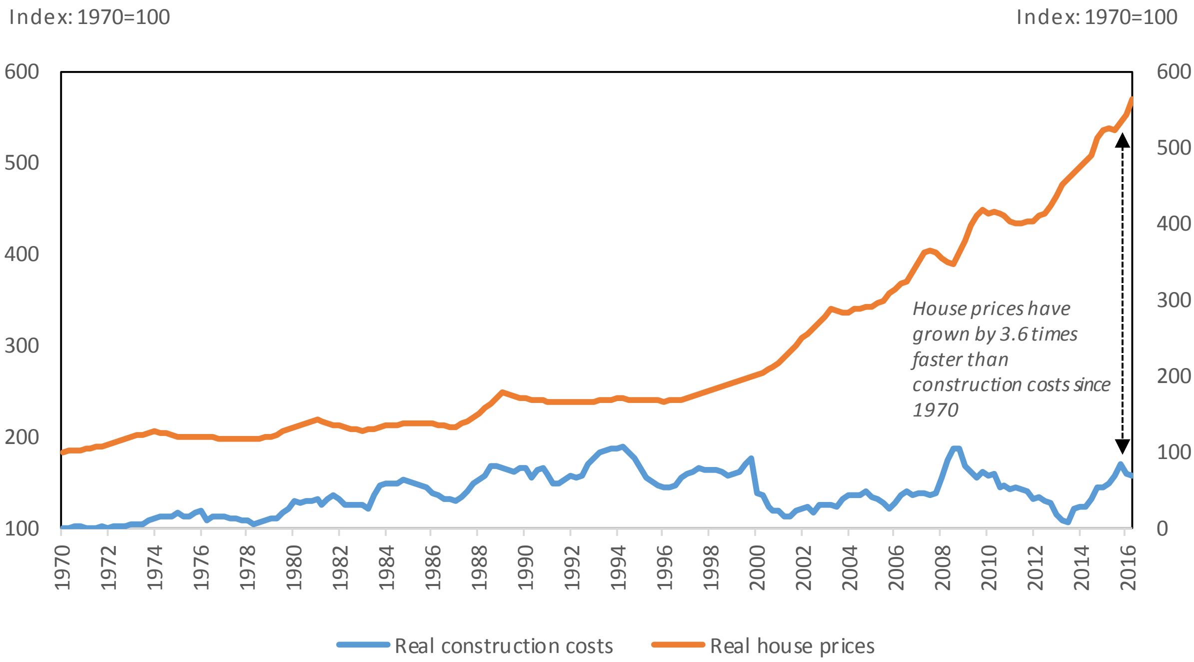
6.4.2 Planning and zoning restrictions, and

6.4.3 Transportation costs

6.5 **Scenario 1: Developer charges and planning delays** make a significant contribution to the cost of new housing developments in the form of charges levied on new land developments for utility, transport, communication and other supporting infrastructure. In addition, embedded land costs, including land shortages caused by inadequate land release policies, planning delays as well as other inputs costs all contribute to increasing the costs of development.

6.6 Traditionally, the cost of developing supporting infrastructure was paid for by Governments. However, these charges are now largely passed onto new perspective home owners. As a result, land prices have grown by a rate almost four times faster than the cost of construction, as shown in the chart below. In turn, growth in the price of land has been the single biggest contributor to the rising costs of new housing developments.

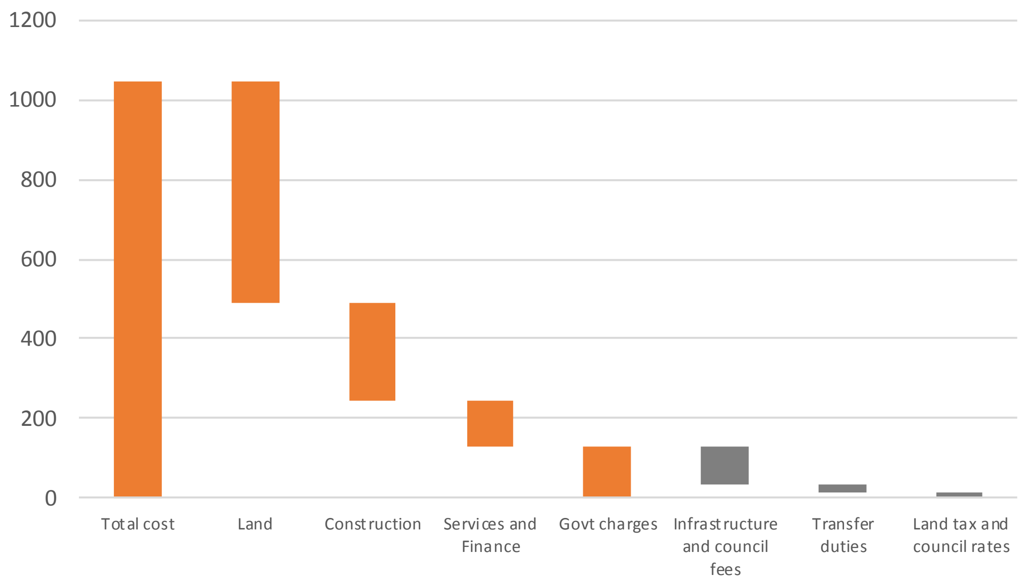
Real construction cost and house price indexes



6.7 In Sydney it is estimated that government infrastructure charges alone contribute 12 per cent to the cost of a greenfield new housing development and 5 per cent to an infill two bedroom apartment, while the average across Sydney, Melbourne, Brisbane and Perth is 7 per cent and 4 per cent respectively.

6.8 As the chart below shows, developer charges in a Sydney greenfield development regularly exceed $100,000, while adding in the 'embedded' costs in land development, including regulated shortages and planning delays, can amount to an additional $300,000.

Development inputs costs ($ '000), Sydney greenfield development



6.9 The analysis assumes these costs can be reduced in two ways (1) by cutting developer charges revenues across the country by $500 million (a fraction of the total impost from developer charges nationally) or (2), that planning processes can be reduced by one month for new housing developments. In doing so it assumes that a $500 million reduction in developer charges is equivalent to a one month reduction in planning timelines.

6.10 The economic benefits of reductions in developer charges and delays are compelling. Based on these assumptions, and considered individually, each of these reforms has the potential to add $850 million to Australia's gross domestic product (GDP), in net present value (NPV) terms over the next four years. Household consumption is projected to increase by $1.4 billion in NPV, bringing forward the construction of approximately 36,000 dwellings over this period.

6.11 If both reforms were implemented then you could expect the benefits to increase proportionately, or thereabouts.

6.12 House prices would also be 0.5 per cent lower as a result of these reforms. However, it could; be expected that if greater reductions in developer charges or planning delays were achieved that they would be accompanied by a relative reduction in house prices. For example, if developer charges were reduced by further, say by $2 billion (still a relatively small fraction of total developer charges) then house prices would fall by a comparable amount.

6.13 When considering the case for reductions in unnecessary delays in the planning process, the case for reform is particularly compelling as it comes with no first-round reduction in public sector revenues, and indeed would likely increase government revenues in line with increased activity.

6.14 While for some development types and some areas a one month improvement may not be possible, this scenario leaves available other alternate improvements including reductions in other regulatory costs in the development of new residential land.

Impacts of reduced developer charges or planning delays

	NPV/average	2017/18	2018/19	2019/20	2020/21
GDP ($m)	851	107	251	312	363
Household consumption ($m)	1,400	243	486	477	470
Employment (FTE)	1,216	714	1,417	1,379	1,353
Investment ($m)	2,934	604	1,123	945	808
Construction activity ($m)	1,955	400	746	631	543
Construction jobs (FTE)	2,193	1,537	2,837	2,376	2,022
Dwelling completions		15,820	32,985	34,584	36,074
NSW		*4,978*	*10,380*	*10,883*	*11,352*
VIC		*4,094*	*8,536*	*8,950*	*9,336*
QLD		*3,128*	*6,522*	*6,838*	*7,133*
SA		*1,069*	*2,229*	*2,337*	*2,438*
WA		*1,778*	*3,706*	*3,886*	*4,053*
Tas, NT, ACT		*773*	*1,611*	*1,689*	*1,762*

Source: Cadence Economics Estimates

Notes: All figures are shown as deviations from a counterfactual baseline. NPVs calculated using a 7% discount rate

6.15 **Scenario 2: The impacts of zoning restrictions** can place significant constraints on the achievable population density, particularly in inner city areas where the cost of travel is the lowest and desire to live is highest. Policies to limit housing density (such as building height or plot ratio restrictions) reduce the supply of housing to people in those areas, placing upwards pressure on housing prices in inner city regions and shifting the population further towards the urban fringe.

6.16 This shift outwards has two impacts – in the first instance, it increases the level of urban density in the mid and outer city regions. In the second instance, the inner city supply restriction and the shift outwards of the population increases house prices across the entire city, both due to the supply constraint in the inner city and due to the demand increase in the mid to outer city region.

6.17 While there are a range of good reasons for imposing zoning restrictions, the potential for significant welfare costs to householders must be considered against the intended amenity (benefits).

6.18 For example, the RBA discussion paper *Urban Structure and Housing Prices: Some Evidence from Australian Cities* finds that in a city of two million people, relaxation of height constraints by one story decreases house prices near the CBD by around 10 per cent, increasing to a 13 per cent reduction for a city of four million persons.

6.19 Subsequent research by Cadence Economics, using a similar analytical framework to that used in the aforementioned RBA discussion paper, focussed specifically on the distribution of how zoning impediments are experienced in cities of different sizes. Zoning restrictions are often most binding in larger cities where the financial incentives for building to (for example) high plot ratios and multiple stories are the highest.

6.20 Considering comparable zoning restrictions between large, medium and small cities, housing prices fall by 2.31 per cent in a big city (> 4 million people). By comparison, in a medium city this same shock leads to a 1.47 per cent decrease, while in a small city the impact is 0.53 per cent.

6.21 The potential economic impacts of zoning reform are significant, with a net present value of household consumption of over $500 million and an additional 20,000 dwellings estimated to be built over the next four years as a direct result.

Impacts of zoning restrictions

	NPV/average	2017/18	2018/19	2019/20	2020/21
GDP ($m)	323	30	71	120	176
Household consumption ($m)	564	69	137	206	277
Employment (FTE)	498	202	400	597	793
Investment ($m)	1,226	171	317	445	559
Construction activity ($m)	816	113	211	296	373
Construction jobs (FTE)	935	434	800	1,114	1,390
Dwelling completions		4,472	9,312	14,513	20,076
NSW		*1,673*	*3,483*	*5,428*	*7,509*
VIC		*1,408*	*2,933*	*4,571*	*6,323*
QLD		*619*	*1,289*	*2,009*	*2,778*
SA		*258*	*538*	*838*	*1,159*
WA		*395*	*822*	*1,281*	*1,772*
Tas, NT, ACT		*119*	*248*	*387*	*535*

Source: Cadence Economics Estimates

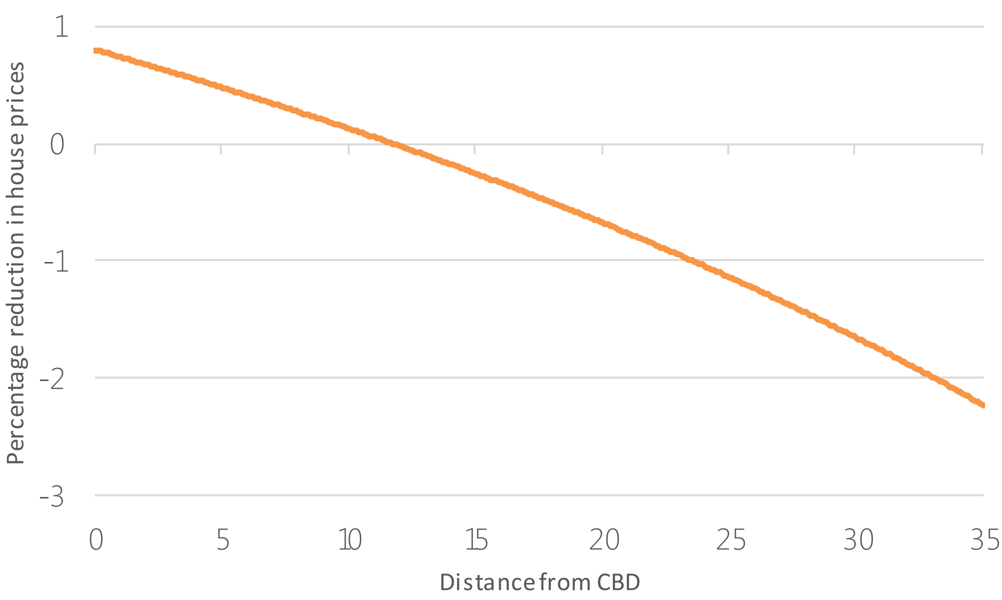
Notes: All figures are shown as deviations from a counterfactual baseline. NPVs calculated using a 7% discount rate

6.22 **Scenario 3: Transportation costs** are a significant component of household expenditure in cities. The cost of travelling between a place of residence and place of work is a major factor in deciding where to live – for example, near the CBD (or nodes on transport networks) the price of housing will be high, however the cost of transport will be low, while at the urban fringe the opposite holds.

6.23 Targeted investment in transport infrastructure can help to reduce transport costs through, for example, reducing road congestion or increasing carrying capacity and reach of rail and other public transport networks. This downward pressure on the cost of transport improves the viability of living further from work, allowing more of the population to live further from the CBD and in turn reducing price pressure for housing closer to the CBD.

A fall in transport cost of 1% across an entire city (as shown below) will cause housing prices to fall for all housing within 12 kilometres of the city CBD, due to a lower opportunity cost of transport.

Price impact of a 1% fall in transportation costs across a city



6.24 But perhaps the greater contribution from having better transport infrastructure comes in the form of increased future housing supply, by unlocking more well-located land and putting downward pressure on prices as the supply of new housing increases.

6.25 Using the detail provided in the cost benefit analyses undertaken for the M4, WestConnex and Melbourne Metro we estimate that private transport benefits account for 24 per cent of the total transport benefits of a representative transport infrastructure project, with an investment of approximately $254 million required to reduce the average travel cost per km by 1 per cent.

6.26 For the purposes of this analysis we assume that fifty percent of the $1 billion National Housing Infrastructure Facility is used on transportation projects, and from the funding allocated to support state infrastructure projects we assume only the Roads to Recovery and fifty percent of the Road component of the Infrastructure Investment Program contributes to reduced travel time for householders.

6.27 The impacts of the budget measures make a $1.15 billion contribution to aggregate household consumption, and add approximately 38,000 houses to the national housing stock.

Impact of reduced transportation costs

	NPV/average	2017/18	2018/19	2019/20	2020/21
GDP ($m)	688	83	167	270	319
Household consumption ($m)	1,145	182	309	436	457
Employment (FTE)	998	535	897	1,254	1,305
Investment ($m)	2,418	449	693	899	864
Construction activity ($m)	1,611	297	461	599	578
Construction jobs (FTE)	1,823	1,142	1,751	2,253	2,146
Dwelling completions		11,972	22,468	32,290	38,368
NSW		*3,882*	*7,285*	*10,470*	*12,441*
VIC		*3,167*	*5,943*	*8,541*	*10,148*
QLD		*2,252*	*4,226*	*6,074*	*7,217*
SA		*825*	*1,548*	*2,224*	*2,643*
WA		*1,330*	*2,497*	*3,588*	*4,264*
Tas, NT, ACT		*516*	*969*	*1,393*	*1,655*

Source: Cadence Economics Estimates

Notes: All figures are shown as deviations from a counterfactual baseline. NPVs calculated using a 7% discount rate

7 Recommendations for Immediate Implementation

7.1 Master Builders priority areas for immediate reform are expressed in detail in our 2017 pre-Budget submission and are listed below under the sub-headings of housing affordability and infrastructure investment.

7.2 Added to this are recommendations derived through subsequent research into the challenges for housing affordability and housing construction across and within different cities in Australia.

7.3 The research found in two Master Builders reports into the housing sector and cities development; (1) *Unlocking Supply: keeping home ownership within reach of all Australians* (2017), and (2) *Consideration of Measures Aimed at Improving Housing Supply*[6], provides an example of the potential benefits of reforms and is intended to provide a basis for policy decision to be made in terms of the allocation of funding into increased housing supply and a framework for potential incentive payment to follow through an assessment of priority issues in the housing sectors in different states/territories.

7.4 Additionally, Master Builders recommends the immediate implementation of proposed reforms under the Henry Tax review (2010), namely:

Recommendation 69: COAG should place priority on a review of institutional arrangements (including administration) to ensure zoning and planning do not unnecessarily inhibit housing supply and housing affordability, and

Recommendation 70: COAG should review infrastructure charges (sometimes called developer charges) to ensure they appropriately price infrastructure provided in housing developments. In particular, the review should establish practical means to ensure that these charges are set appropriately to reflect the avoidable costs of development, necessary steps to improve the transparency of charging and any consequential reductions in regulation.

7.5 Master Builders also supports a number of recommendations of the Harper Review into Competition Policy, which provide a short-list of guiding principles to follow when forming better targeted cities development policy. Notably,

Recommendation 1 – competition principles: Master Builders endorses all elements of this recommendation with a call to governments at all levels to "*laws and institutions which promote the long-term interests of consumers*"

Recommendation 8 – Regulation review: All Australian governments should review regulations, including local government regulations, in their jurisdictions to ensure that unnecessary restrictions on competition are removed. Legislation (including Acts,

[6] These two reports were developed by Cadence Economics using their computerized general equilibrium modelling framework to examine the economic contribution of reforms which boost the supply of new housing.

ordinances and regulations) should be subject to a public interest test and should not restrict competition unless it can be demonstrated that:

- the benefits of the restriction to the community as a whole outweigh the costs; and
- the objectives of the legislation can only be achieved by restricting competition.
- Factors to consider in assessing the public interest should be determined on a case-by-case basis and not narrowed to a specific set of indicators.

Recommendation 9 – Planning and zoning: state/territory governments should subject restrictions on competition in planning and zoning rules to the public interest test, such that rules should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs.

- An independent body, such as the Australian Council for Competition Policy should be tasked with reporting on performance across the levels of government.

Housing Affordability

7.6 Introduce payments to higher-performing local governments based on national competition policy principles, with the aim of encouraging improved delivery of housing related services, amenities and infrastructure.

7.6.1 Areas of reform should be flexible and tailored to the needs of housing market across different jurisdictions. Master Builders recent report; *Consideration of Measures Aimed at Improving Housing Supply* offers a list of priority issues facing housing markets in different state/territories in Australia. The report can be found as part of the attached documentation to this submission.

7.7 Streamline and simplify development approvals processes for residential developments, with a greater reliance on a code-based assessment and identification of best practice development approvals processes in state/territory and local government.

7.8 State/territory and local governments to develop and implement tailored Land Release Plans. This would include identifying ways to overcome regulatory or other impediments to the supply of new land zoned for residential development.

7.9 Develop an annual publication of developer charges applied by all local governments in Australia. This would not leave anywhere for overcharging local governments to hide and would increase the transparency between infrastructure charges and infrastructure costs.

7.10 Improve access to affordable housing, through increased funding and alternative funding models and better collaboration across the different levels of government and the private sector.

Infrastructure

7.11 Prioritise infrastructure investment, through the $1 billion National Housing Infrastructure Facility and the $75 billion infrastructure investment package, to focus on infrastructure projects which unlock new land for residential development. This should, if possible, focus on greenfield developments inside existing city boundaries and seek to provide additional residential land in high demand areas. Unlocking more affordable land for residential development is the first step in developing a more sustainable housing stock in the long run.

7.12 Seek more innovative ways to provide residential infrastructure. In the past this infrastructure was provided by government. Today this infrastructure is largely provided by private developers, with the cost of development passed onto prospective homeowners (including with profit). The latter is a major reason why land prices have increased by almost six times in the last forty years.

7.13 Transport infrastructure is critical in unlocking land for development. People will live where there commute times are the lowest, relative to what they can afford. Better transport infrastructure can transform a city allowing people to live closer to where they work, reducing commute times and costs and improving living standards.

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Master Builders Australia

2017-18 PRE-BUDGET SUBMISSION

March 2017

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CONTENTS

1 Master Builders Australia

1.1 Master Builders is the peak national association for the building and construction industry in Australia. Master Builders' primary role is to champion the interests of the building and construction industry, representing residential and commercial building, and engineering construction.

1.2 Master Builders has more than 32,000 member-companies with representation in every State and Territory in Australia, the great majority of which, by number, are small to medium sized enterprises. Master Builders' membership consists of large national, international, residential and commercial builders and civil contractors through to smaller local subcontracting firms, as well as suppliers and professional industry advisers. Membership of Master Builders' represents 95 per cent of all sectors of the building and construction industry.

1.3 The building and construction industry is the second largest industry in Australia, accounting for 8.1 per cent of Gross Domestic Product and provides jobs for close to 1.1 million Australians - 8.9 per cent of total employment in Australia.

1.4 Owner-occupied housing and other property investments account for over two-thirds of the asset portfolio and wealth of ordinary Australians.

1.5 The building and construction industry is made up of approximately 345,000 businesses of which 95 per cent are small businesses and independent contractors. Combined, these businesses employ 670,000 workers including 70,000 apprentices.

1.6 The cumulative building and construction task over the Budget forward estimates will require work done to the value of $723 billion and for the number of people employed in the industry to rise by 5.3 per cent to 1.15 million.

1.7 This pre-Budget submission sets out Master Builders proposed approaches to addressing these (taxation reform; fiscal consolidation), and other (for example, housing affordability, workplace productivity and skills, and regulation reform) economic policy issues.

2 Main Recommendations

Fiscal Strategy

1. **Develop and deliver on a clear path to a Budget surplus.** This must involve eliminating waste and inefficiency from public spending, and ensuring fiscal settings have a neutral impact on interest rates
2. **Implement the *ten year enterprise tax plan***, *with the aim of reducing the ten year time horizon if and when economic conditions and the Budget allow.*
3. Developing more **innovative funding arrangements for public and private infrastructure** projects
4. As a priority Master Builders supports the implementation of **competition payments from the Commonwealth to the state/territory Government's** for the implementation of reforms, particularly in the property sector, that promote greater competition and make the tax system more efficient – consistent with **Recommendation 48 of the Harper Review (2015)**
5. Master Builders endorses **Recommendation 8 of the Harper Review – regulation review.** All Australian Governments should review regulations, including local Government regulations and **eliminate 'red' and 'green' tape costs and compliance burdens were possible.**

Taxation

6. **Reducing the company tax rate to 25 per cent to increase the competitiveness of Australia's tax settings** – this is must be a first priority to keep Australia's business environment competitive against international standards
7. **Closing the gap between the company tax rate and the higher personal income tax rates**
8. **Abolish stamp duty** on business conveyances, as promised in the 1999 Intergovernmental Agreement on the reform of Commonwealth-State Financial Relations
9. A review of the costs/benefits of **reducing stamp duty on the sale of residential property** to first home buyers
10. **Eliminating the cumulative impact of the Goods and Services Tax (GST).** Specifically, stamp duty should be levied on the GST exclusive price of property and land. Not doing so is imposing 'a tax on a tax'.

11. Reforming developer (infrastructure) charges through the offer of **competition payments that compensate State and local governments** and councils for implementing policy that reduces the tax burden on new residential developments.

Housing Affordability

12. Introduce **payments to higher-performing local governments** based on national competition policy principles, with the aim of encouraging improved delivery of housing related services, amenities and infrastructure.
13. **Streamlined and simplified development approvals** processes for residential developments, with a greater reliance on a code-based assessment and identification of best practice development approvals processes in state/territory and local government.
14. State/territory and local governments to develop and implement **tailored Land Release Plans**. This would include identifying ways to overcome regulatory or other impediments to the supply of new land zoned for residential development.
15. Creating a genuine, comprehensive and enforceable **uniform building code and regulatory system**. COAG must play a leading role in developing the BCA into a nationally consistent central authority for building and construction across all jurisdictions.
16. Ensuring state/territory governments honour their commitment to **abolish stamp duties** on business conveyance of real property.
17. **Develop and annual publication of developer charges applied by all local governments in Australia**. This would not leave anywhere for overcharging local governments to hide and would increase the transparency between infrastructure charges and infrastructure costs.
18. **Improve access to affordable housing**, through increased funding and alternative funding models and better collaboration across the different levels of government and the private sector

Small Business

19. Delivery a **small business-friendly environment** and boosting confidence through stable economic settings.
20. **Security of payments for subcontractors** through policy that protects subcontractors from taking on the implicit business risks of their larger contracting counterparts.
21. Targeted measures to **assist small business employers to take on more apprentices** and help to increase the completion rates for building trade apprentices.
22. **Streamlining the development approvals processes** to help smaller business stem the growing shortfall in new housing supply.

23. **Simplified tender processes and reduced costs** to encourage more small businesses participation in government funded building and construction projects.
24. **Reviewing current regulation at all levels of government** in terms of their real economic cost, with the aim of removing inefficient regulations that bare a high economic cost – regulators should approach regulatory review and removal with the same level of vigour given to the implementation of new regulation.
25. **Subject all new regulations to a transparent and rigorous cost-benefit** analysis framework that is endorsed by the Productivity Commission and is subject to public scrutiny.
26. **Simplify business tax compliance**, recognising that inefficient collection and administration of taxes distorts economic decision making and capital investment.
27. **Assist small businesses by reducing the broader complexity of taxation and industrial relations laws**, tackle the compliance costs of regulation - which too often form an indirect competitive disadvantage for small businesses compared to large businesses – increase their ability to access debt and equity finance and do more to facilitate their participation in government procurement.

Workplace Programs and Agencies

28. **Proper resourcing for the Australian Building and Construction Commission (ABCC)** to properly fulfil its increased mandate to; increase productivity, reduce disputes and delays, foster greater cooperation between workers and employers on commercial building sites and the economy in general
29. **To keep the remit of the ABCC to that outlined above**. **Issues pertaining of 457 visa's** and visa holders, as well as the scope of their application should be left to the appropriate government department and **should not form part of the remit of the ABCC**
30. **Preserve the rights of independent contractors** by retaining the current laws that give people choice about how they work and encourage entrepreneurship
31. **Ensure the Registered Organisations Commission (ROC) is properly funded** and focused on ensuring building union officials are held to a standard that is consistent with those expected from our business leaders and elected officials
32. Adopt **a workplace bargaining system in which employers and employees can freely enter into appropriate and lawful workplace agreements**, underpinned by simple safety net conditions. Employers and employees must be the two most important parts of an employment relationship. **The role of third parties should only exist where invited** and must never take precedence over the wishes of employees or employers

33. **Implement fair and simple dismissal laws that place more emphasis on the right of employers** to manage their own business, reflect community expectations and embrace the notion of 'common sense'
34. Continue to pursue **nationally consistent workplace safety laws** and increase the focus on practical safety outcomes and a safety orientated workplace culture
35. **Stop and reverse the growth in overlap between safety laws and industrial relations laws**
36. **Ensure that the concept of workplace safety is not further sullied** by prohibiting notions of 'safety' from being exploited as a tactic to achieve industrial relations outcomes
37. **Review the operation and work of Safe Work Australia** to reduce duplication with other bodies, focus operational activity and improve engagement with employers, including through the appointment of more business representatives to its board
38. Master Builders supports the **Harper Review recommendation (Recommendation 36) on the prohibition of secondary boycotts** in sections 45D-45E of the *Competition and Consumer Act (2010)* to be maintained.

Workforce Skills

39. Targeted measures to **assist and encourage employers to take on more apprentices** and to increase the completion rates of building trades apprenticeships, including the return of, and increases to previously available incentive programs
40. **Targeted pre-apprenticeship programs** that support site-ready and productive apprentices to boost business productivity and improve safety in the workplace
41. Significantly boost **financial assistance to building and construction industry employers who invest in the training and mentoring** of young people while completing their apprenticeships.
42. Greater support for industry led programs to **increase female participation in the building and construction industry**
43. **Improved investment in VET** to give young people access to publicly funded industry-focussed training upon completing year 12
44. **Review the national VET training system** to remove current complexities, increase business and parent understanding, and implement consistent funding models
45. **Provide industry with a greater role in determining quality training outcomes from RTOs** by allowing industry to provide feedback on their performance
46. Better support for **mentoring programs** that are proven to increase apprenticeship completions

47. More support for **partnership programs between VET and tertiary education providers**, specifically to develop pathways between construction trades and engineering and construction management higher education degrees

Infrastructure

48. Increase private sector investment in infrastructure**, with a target of 6 per cent of GDP for public infrastructure investment across all levels of government.**

49. Expand the use of privitisation models. **Revenue from the sale of existing infrastructure assets should be used to fund the development of new infrastructure.**

50. Developing and marketing tradable public infrastructure bonds **on terms of trade and conditions which appeal to a broader spectrum of investors.**

51. Redirection of government outlays away from recurrent and less productive spending, toward investment in efficiency and competitiveness enhancing infrastructure**.**

52. Better policy coordination among the levels of government. **The Federal Government should lead a plan, through COAG, to address Australia's growing infrastructure needs.**

53. Minimising bid costs for infrastructure supply and financing to ensure the broadest possible range of engagement by potential investors. Tendering processes for smaller investors should be simplified.

54. Reducing the political risk associated with investment in infrastructure. **This would involve focusing on 'stop-start' government decision making, and the tendency for the constant changing of processes, rules and other key elements of a project once underway.**

55. Master Builders supports measures outlined under **Recommendation 9 of the Harper Review**. *"State and territory Governments should subject restrictions on competition in planning and zoning rules to the public interest test, such that the rules should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the rules can only be achieved by restricting competition."*

56. Master Builders supports a recommendation to **review Government procurement policies and policies pertaining to other commercial arrangement with the private sector**, including procurement policies, commissioning, private-public partnerships and privatisation guidelines – **Recommendation 18 of the Harper Review** (2015)

Immigration

57. Setting the **permanent migration intake at 240,000 per year**, with a focus on skilled migration
58. **Reducing the visa sponsorship period for employer-nominated visas from three to two years**, to help employers engage in the construction of large projects
59. **Review the 'highly skilled' threshold within employer-nominated visa classes** to reduce ongoing skills shortage in 'middle and semi-skilled' occupations and resulting project bottlenecks

3 Introduction

3.1 2017 is shaping up to be a year of increased political and global volatility. In that context Australia's economic risks are rising, and we should be raising our defences. This makes the task of Budget repair even more urgent.

3.2 The building and construction industry has been a key driver of the Australian economy through a period of transition and has played an important role in helping the economy make the switch from the mining investment boom.

3.3 It is the second largest industry in Australia and employs over 1.1 million people. But it is also one of the highest taxed industries, with taxes and charges levied at all three levels of government, raising the cost of building our homes, schools and hospitals.

3.4 Master Builders in this submission seeks the Government to consider the *Strong Building Strong Economy* policy priorities, and to strive for a policy framework that helps businesses in the building and construction industry prosper and grow, to do what they do best – building more houses, hospitals and roads, train apprentices and provide more skilled jobs for Australians. Master Builders policy priorities, as set out in the following sections of the submission cover the areas of taxation, fiscal strategy, housing affordability, small business, infrastructure, workplace relations, workforce skills, and immigration.

3.5 Master Builder's tax reform priorities are expressed in a number of detailed submissions to the Government including as part of our Strong Building Strong Economy 2016 pre-election campaign, as well as in response to calls for input into the Submission to the Treasury's Affordable Housing Working Group (2016), the "Re: Think: Tax Discussion Paper" (2015), and previously in response to the finding of the Henry Tax Review (2010). Our tax reform priorities remain largely unchanged given the lack of implemented policy changes to come out of the Governments White Paper and subsequent discussion papers. Our policy position remain consistent and include:

3.6 Safe and Productive Workplaces: Our industrial relations system must be balanced, fair and simple, starting with the proper funding to ensure the re-established Australian Building and Construction Commission (ABCC), with its additional remit responsibilities to enforce and prosecute on its mandate to bring the rule of law back to Australian building site.

3.7 Affordable Housing: Keeping homeownership within reach of everyday Australians, through more affordable housing options to reduce the cost of living and improve opportunities for more families and young people to buy their own home. Negative gearing rules must stay.

3.8 Jobs and Skills for the Future: Better investment in skills and apprentice training to satisfy the growing demand for construction and trade skills, and to avoid future skills and labour shortages.

3.9 Economic Settings for Stability and Growth: Overhauling the tax system and adopting a responsible approach to structural Budget repair that gives confidence to consumers and investors, and establishes a lasting, long-term economic strategy based on sounds economic principles.

3.10 More Infrastructure and Investment: Greater cooperation between public and private sectors to fund investment in urban and regional infrastructure.

3.11 More Small Business and Less Red-Tape: Increased emphasis on the needs of small contractors by continued cuts to red-tape and regulation.

4 Economic Overview

A business-friendly environment is essential for a stronger economy and more jobs

4.1 The challenge is to build on Australia's record run of 25 years of uninterrupted economic growth. Our economic performance over the past three decades has been exemplarily and the envy of other developed countries around the world and must be seen as a platform and an opportunity for securing our future in what is shaping up to be a more volatile economic and geo-political environment.

4.2 As a result of uninterrupted economic growth most Australians are better off now than any other time in our history. But we cannot rely on our past success, we cannot rest on our laurels nor rely on the rest of the world to secure our future prosperity.

4.3 The objective must be maintain our rate of growth in living standards, by implementing economic reforms that support productivity growth in the economy.

4.4 While fundamentally sound, the Australian economy faces a number of mounting challenges. For growth to be sustained over the long run, fiscal discipline is needed to bring the structural Budget back in balance, and to address rising Government deficit and debt. The imposition of more and higher taxes must not be the baseline policy position. Instead the Budget setting must be geared towards promoting long run economic growth that is supported by a range of reform measures. Structural reforms to our taxation system and to Government expenditure must be a priority of our fiscal policy to support long run, sustained economic growth.

4.5 The urgent need for structural Budget repair was highlighted by the September quarter 2016 National Accounts, which showed a contraction in GDP of 0.5 per cent.

4.6 Master Builders acknowledges that the Australian economy continues to undergo a period of adjustment following the global financial crisis and the resources investment boom. Historically, boom periods are followed by busts in relatively equal portions. But the unwinding of the past resource investment cycle has been relatively smooth but incomplete.

4.7 At the same time, it is important for Government to support, through ongoing structural reforms, those sectors which are well placed to make an immediate and positive contribution to the economy, productivity and employment. The building and construction industry is one such industry well positioned to support economic growth:

- The building and construction industry is the second largest industry in Australia, accounting for around 9 per cent of Gross Domestic Product and provides jobs for close to 1.1 million Australians – approximately 9 per cent of total employment in Australia.
- The cumulative building and construction task over the Budget forward estimates will require work done to the value of $723 billion and for the number of people employed in the industry to rise by 5.3 per cent to 1.15 million.
- The building industry is also a 'horizontal' industry in the sense that building and construction work provides the physical capital for other industry to prosper and grow, as well as the shelter for workers and the wider Australian population.
- The industry has deep supply chains through other industries such as manufacturing, transport, wholesale and retail and is the single biggest industry consumer of raw materials in the economy.

4.8 Master Builders sees a number of risks to the official forecasts. Official forecasts in the 2017 MYEFO assume revenue growth recovering, with average gains of approximately 5 per cent per year to 2019-20. But with GDP falling in the September quarter 2016 and rising global volatility, including a trend towards more protectionist trade policies, there is a risk that the economic rebound may not be as strong and as a consequence act as a dampener on the Budget, causing revenue to undershoot official estimates.

4.9 Growing global political and economic volatility makes the domestic reform agenda urgent. Fiscal policy must take a greater share of the heavy lifting in supporting and sustaining long run economic growth. Australia's trade relationship with China is now more closely tied than any previous two way trade relationship in our history. But China faces economic challenges of its own in the coming decade, with the resulting impacts a direct risk to Australian economic prosperity.

4.10 Despite global volatility and ongoing structural adjustments, the domestic outlook remains positive. Master Builders expects Real GDP to grow by 2.7% next year followed by average growth of 3.2% per year over the forward estimates. A strong building and construction industry will be a critical element in support this economic growth. Over the forward estimates the building and construction industry is slated to support $1.1 trillion in business and infrastructure investment, which will provide jobs for over 1.1 million Australians.

5 Building and Construction Industry Outlook

A strong building and construction industry is vital to a strong economy. It creates jobs, trains apprentices, drives wider economic growth and builds better communities

5.1 The building and construction is the second largest industry in Australia. It contributed around 9 per cent of GDP in 2015-16 and provides rewarding, well-paying careers for over 1.1 million Australians, representing approximately 9 per cent of the Australian workforce. The Building and construction industry must remain a key industry driver of economic growth and jobs in 2017-18 and beyond.

5.2 Master Builders takes the 'pulse' of the building and construction industry through its quarterly National Survey of Building and Construction. The Survey provide a snapshot of sentiments of industry participants across all sectors of the building and construction industry; residential, renovations, commercial building, engineering construction, sub-contracting and building materials suppliers.

5.3 The short term outlook for the building and construction industry is optimistic amongst industry players, with most metrics of performance showing positive sentiments or signs of improvement. For instance:

- business confidence improved significantly in December 2016, driven largely by a return to more positive sentiments for non-residential builders;
- by sector, both residential and non-residential builders see further strengthening in activity levels over the coming six months, with the index for future building activity now more positive for non-residential builders than for residential builders;
- Business conditions improved during the second half of 2016, driven by higher profits and an improvement in sales contracts. Hiring intentions recorded their best quarter result in more than two years, and the reintroduction of the ABCC was noted as a positive, particularly for builders in the non-residential and engineering construction sectors.

- However, sentiments do vary considerably by state/territory with NSW and Victoria leading the positive outlook, while Western Australia, Queensland and the Northern Territory continue to face challenges as resources related building activity continues to fall.

5.4 Master Builders also prepares its own Building and Construction industry forecasts. The forecasts show a period of transition ahead with the three major industry sectors of building and construction – engineering, non-residential, and residential construction – all at very different stages in their investment and construction cycles.

5.5 **Residential building** is expected to peak in the next 12 months, but not before a record building effort in 2016-17, with the total value of new homes construction expected to reach $66.7 billion and renovations expected to contribute an additional $7 billion.

5.5.1 This upturn has been driven by a number of factors, including sustained low interest rates, the availability of first home owner grants which favour new ahead of established dwelling, and strong demand from both domestic and foreign investors.

5.5.2 Dwelling commencements are expected to moderate earlier, to a projection for 206,900 new dwelling commencements in 2016-17 – a fall of 9.9 per cent on the record number of 229,500 commencements recorded in 2015-16.

5.5.3 In terms of the value of work done, residential building activity should be well into a period of consolidation by 2017-18, with activity forecast to fall by 10.1% ($7 billion) during the year.

5.5.4 Over the forward estimates, the residential building task is significant, with the combined value of construction work to 2020-21 projected at over $314 billion (in 2013-14 prices), and includes the construction of over 900,000 new dwellings.

5.6 The **non-residential building** activity is expected to be soft in 2016-17, with the value of work done expected to fall by 10 per cent during the year. But the outlook presents more positive prospects, with non-residential building activity expected to record growth in each of the remaining years of the Budget forward estimates. On average, non-residential building activity is expected to growth by 1.7 per cent per year over the next four years, with the total value of non-residential building work to reach $34.1 billion in 2020-21.

5.6.1 Master Builders expects total commercial building work done to drop 18%, in real terms, over 2015-16 and 2016-17.

5.6.2 Office building is expected to decline by 28.5% in 2016-17, while health, transport buildings, retail and other commercial & industrial building will also fall significantly in 2016-17 and 2017-18.

5.6.3 On the other hand, areas of strength over the next year include agriculture and aquiculture (13.4%), accommodation (11.2%) and warehousing (8.6%).

5.7 The **engineering construction** sector continues to undergo a painful transition following almost a decade of boom conditions, driven by major investment into expanding mineral and gas production capacity. The latter is expected to weigh negatively on the value of broader engineering construction in 2016-17, with engineering construction work forecasts to fall by $17.3 billion (-18.4 per cent), as the last of the major LNG projects in Western Australia and Queensland are completed. Looking ahead, engineering work is expected grow by 7.4 per cent in 2017-18 and expand in each of the following years of the forward estimates.

5.7.1 The downturn in resources investment will continue through 2017-18, driven from this point onwards by a big decline in LNG and related gas field and pipeline work. Over the two years from 2015-16 to 2017-18, resources related construction work is forecast to fall by more than half, taking more than $22 billion worth of resource related construction activity out of the economy.

5.7.2 Transport infrastructure construction work is forecast to be over $6 billion higher in 2016-17 than the previous year, growing by 29.8%. Over the four years to 2019-20 the total value of transport related construction is projected to be upwards of $132 billion, outdoing resources related investment by a ratio of almost 2:1 and accounting for $2 in every $5 spent on engineering construction investments in Australia over the next four years.

5.8 **Challenges ahead** are mounting, with the three main sectors of the building and construction industry all facing, to varying degrees, the same wider economic challenges and risks:

- Increased global volatility and emergence of protectionist trade policies;
- the future direction for China's economy and Chinese policy on capital controls, given its significance as a destination for our exports (of both commodities and services), and a major source of capital investment;
- the future direction of interest rates, which play an important role in home-buyer and business investor decision-making, as well as individual's debt servicing power;
- Added to this is the risk that Australia loses its AAA credit rating. Doing so may raise the cost of capital and reduce access to capital at a time when private business investment in Australia is in desperate need of stimulus. Last time Australia lost its AAA credit rating it took almost two decades to get it back. This may also take some power away from monetary policy if retail banks are forced to raise mortgage rates or not pass on potential future cuts to the official cash rate. Losing the AAA credit rating would also cause interest on Government debt to rise and may impact the path back to a balanced Budget.

5.9 Another important driver of demand for buildings and homes is population growth. A T clearly stated medium to longer term net overseas migration intake, which is likely to account for almost 60 per cent of our population growth, would help in the planning process and would give building and construction business greater clarity to make long term business decisions about how and where they should be investing resources. By setting a consistent migration target of 240,000, we lock in the trajectory of population growth and have a much better idea about the future demand for infrastructure, commercial and social buildings, and housing. .

5.10 Master Builders recognises global economic conditions and prospects of the Chinese economy are largely outside the field of influence of the Australian Government. However, the other three – interest rates, Australia's AAA credit rating, and the migration program – are within scope.

6 Fiscal Strategy

Addressing Australia's structural Budget deficit and adjusting economic policy settings will help restore confidence to investors and consumers

Policy Recommendations

60. **Develop and deliver on a clear path to a Budget surplus.** This must involve eliminating waste and inefficiency from public spending, and ensuring fiscal settings have a neutral impact on interest rates
61. **Implement the *ten year enterprise tax plan***, *with the aim of reducing the ten year time horizon if and when economic conditions and the Budget allow.*
62. Developing more **innovative funding arrangements for public and private infrastructure** projects
63. As a priority Master Builders supports the implementation of **competition payments from the Commonwealth to the state/territory Government's** for the implementation of reforms, particularly in the property sector, that promote greater competition and make the tax system more efficient – consistent with **Recommendation 48 of the Harper Review (2015)**
64. Master Builders endorses **Recommendation 8 of the Harper Review – regulation review.** All Australian Governments should review regulations, including local Government regulations and **eliminate 'red' and 'green' tape costs and compliance burdens were possible.**

6.1

6.2 Master Builders sees it as an imperative for the Government to prioritise Budget measures that maximise opportunities for economic growth through tax and productivity enhancing reforms. This must involve eliminating waste and inefficiency from public spending, and ensuring fiscal settings have a neutral impact on interest rates

6.3 A significant risk is the structural imbalance between Government revenue and spending that has underpinned a period of successive deficits, dating back to 2009.

"Australia has experienced one of the fastest rises in public debt in the world since the Global Financial Crisis (GFC) and federal budget deficits have

persisted for longer than previous fiscal stimulus episodes in the 1980s and 1990s. Subsequent fiscal repair has also been weaker and less than in the United States, United Kingdom, New Zealand and the Euro area." (Makin, 2016)

6.4 The Federal Budget now faces up to 13 years (or more) of consecutive deficits, at a time when economic activity has been relatively healthy. The fiscal deficits we are facing are structural, underpinned by permanent spending promises locked in during a temporary boom period. Hence, tax reform that makes the economy more efficient and sustains long run growth must be a priority.

6.5 The Budget imbalance must be addressed in order to make resources available to support a reform agenda. Specifically, the Treasurer Hon. Scott Morrison has noted that in order to provide competition payments to states/territory Governments to support the implementation of reforms that promote competition and productivity, the Budget must first be in balance and savings measures must pass Parliament. This is a policy position supported by Master Builders.

6.6 Master Builders supports the Government's *ten year enterprise tax plan* that aims to cut taxes for small and medium-sized businesses, boost new investment, and supports growth in jobs and real wages. However the ten year implementation time horizon should be shortened as soon as economic and Budget conditions allow and also be extended to all enterprises regardless of size.

6.7 The Government's investment in the national innovation and science agenda, including financial support for start-ups are supported examples of how to foster new areas of economic growth.

6.8 Master Builders welcomed last year the Government's effort to adjust the personal income tax scale to avoid bracket creep. A tax increase on individuals through bracket creep is inequitable and is a disincentive for individuals to work harder and earn more.

6.9 Master Builders would urge the Government to ensure personal income taxes do not rise as a share of total personal incomes and would encourage the government to implement a long term policy that aims to reduce the marginal personal income tax rates.

6.10 The Government must live within its means. Although Australia's Government debt to GDP ratio is low by OECD standards, at 30 per cent, total debt held by households, the banking sector and the various levels of Government sum up to around 250 per cent of GDP. Government debt is also predominantly owed to foreign bondholders, with foreign debt repayments unmatched by domestic capital accumulation. Government foreign debt can provide a boost to the economy as long as capital is allocated to programs and investments that boost productivity and economic growth. But using foreign debt to service short term spending commitments is unsustainable.

Private Investment in infrastructure

6.11 Master Builders supports the Federal Government's strategy to boost growth through its $50 billion infrastructure package, noting the key role the building and construction sector will play in supporting growth through the delivery of new infrastructure. The government must develop clear and innovative funding arrangements for public and private infrastructure projects.

6.12 However, Master Builders does not support the removal of around $600 million in funding for the Asset Recycling Initiative at a time when Australia is facing an infrastructure shortfall of over $700 billion.

6.13 Over the forward estimates the building and construction industry is slated to support $1.1 trillion in business and infrastructure investment, which will provide jobs for over 1.1 million Australians.

Competition reform

6.14 Master Builders would encourage the Government to allocate funding to implement measures to increase and promote competition in the building and construction industry in the Australian economy more broadly. A number of recommendations have been recently outlined under the Australian Government's Competition Policy Review (the Harper Review, 2015). Master Builders also acknowledges the key principles of competition policy identified under the Hilmer Review (1993):

- *limiting anti-competitive conduct of firms;*

- *reforming regulation which unjustifiably restricts competition;*
- *reforming the structure of public monopolies to facilitate competition;*
- *providing third-party access to certain facilities that are essential for competition;*
- *restraining monopoly pricing behaviour; and*
- *fostering 'competitive neutrality' between Government and private businesses when they compete.*

6.15 Master Builders supports the competition principles as outlined under Recommendation *1 of the Harper Review (2015), including:*

- *Competition policies, laws and institutions should promote the long term interests of consumers.*
- *Legislative frameworks and Government policies and regulations binding the public or private sectors should not restrict competition.*
- *Governments should promote consumer choice when funding, procuring or providing goods and services and enable informed choices by consumers.*
- *The model for Government provision or procurement of goods and services should separate the interests of policy (including funding), regulation and service provision, and should encourage a diversity of providers.*
- *Governments should separate remaining public monopolies from competitive service elements, and also separate contestable elements into smaller independent business activities.*
- *Government business activities that compete with private provision, whether for profit or not for profit, should comply*

with competitive neutrality principles to ensure they do not enjoy a net competitive advantage simply as a result of Government ownership.

- *A right to third party access to significant bottleneck infrastructure should be granted where it would promote a material increase in competition in dependent markets and would promote the public interest.*

- *Independent authorities should set, administer or oversee prices for natural monopoly infrastructure providers.*

6.16 Applying these principles should be subject to a public interest test, such that legislation or Government policy should not restrict competition unless:

- *the benefits of the restriction to the community as a whole outweigh the costs; and*

- *the objectives of the legislation or Government policy can only be achieved by restricting competition.*

6.17 In terms of the efficient provision of public infrastructure - which is discussed in more detail in later sections of this submission – in the context of a broader fiscal strategy, Master Builders policy positon remains consistent with Recommendation 13.1 of the 2014 Public Infrastructure Inquiry. In short the most critical recommendation from the inquiry in the current context is that:

> *Australian, State and Territory Governments should adopt codes and guidelines with an essentially similar framework to the Victorian Code of Practice for the Building and Construction Industry for their own major infrastructure purchases.*
>
> *The Australian Government should require compliance with these guidelines as a precondition for any infrastructure funds it provides to State and Territory Governments.*

Competition Payments

6.18 As a priority Master Builders supports the implementation of competition payments as part of a wider fiscal strategy between the Commonwealth and the State/Territory Governments for the implementation of reforms, particularly in the property sector, that promote greater competition and make the tax system more efficient. The important role that competition payments are likely to play in promoting housing affordability is discussed in later sections in this submission in the context of a wider policy framework for housing affordability.

6.19 There is a case to be made that the benefits of reform, including any fiscal dividend, should be commensurate with the reform effort made. The differing revenue bases of the Commonwealth and the States and Territories mean that revenue may not flow in proportion to reform effort. (Harper, 2015)

6.20 In that context, Master Builders supports the Recommendation 48 of the Harper Review – competition payments. To include:

- *A review by the Productivity Commission into reforms agreed to by the Commonwealth and state/territory Governments to estimate their effect on revenue in each jurisdiction;*
- *Competition policy payments should ensure that revenue gains flowing from reform accrue to the jurisdictions undertaking the reform; and*
- *Reform effort should be assessed by the Australian Council for Competition Policy based on actual implementation of reform measures, not on undertaking reviews.*

6.21 However, such competition payments should only be paid:

- *for 'additionality' – that is, not just for doing what is necessary, but for doing 'more than is required';*
- *based on competition between the States/Territories for a given pool of funds, with disbursements based on agreed targeted areas of reform, promptness and boldness of action against transparent benchmarks; and*
- *only on an ex post basis against proven outcomes and enforceable commitments against recidivist or countervailing behaviour elsewhere.*

6.22 Master Builders endorses an active role for the proposed Australian Council for Competition Policy in assessing reform outcomes (as distinct to reform efforts), and through this channel the quantum and distribution of any competition payments.

Regulation Review

6.23 Master Builders would also highlight, through its commercial arrangements entered into with market participants, the Government (whether in right of the Commonwealth, state, territory or local Governments) has the potential to harm competition and consumer welfare. For example the provision of land by state and local Governments that does not meet short term demand, causing the price of land to be higher than its equilibrium (market efficient) price is anti-competitive and inequitable.

6.24 Master Builder endorses the recommendation of the Harper Review Panel in their conclusion that "the anti-competitive conduct provisions of the Competition and Consumer Act 2010 (CCA) should cover Government activities that have a trading or commercial character." (Harper Review, 2015)

6.25 Master Builders urges the Government to remove regulations that limit user choice and the diversity of product offerings, noting that land and zoning regulation currently place costly restrictions that skew the provision of physical capital in the economy. This is particularly true in the housing market where restrictive land release policies and zoning laws limit user choice, and cause land prices to be above a fair value to the community.

6.26 In this context Master Builders endorses Recommendation 8 of the Harper Review – regulation review. All Australian Governments should review regulations, including local Government regulations, in their jurisdictions to ensure that unnecessary restrictions on competition are removed. Further:

- *Legislation (including Acts, ordinances and regulations) should be subject to a public interest test and should not restrict competition unless it can be demonstrated that:*
- *the benefits of the restriction to the community as a whole outweigh the costs; and*
- *the objectives of the legislation can only be achieved by restricting competition.*

Factors to consider in assessing the public interest should be determined on a case by case basis and not narrowed to a specific set of indicators.

7 Taxation

The building and construction industry is one of the most intensely regulated industries in Australia. This adds to the cost of building homes and community infrastructure

Policy Recommendations

65. **Reducing the company tax rate to 25 per cent to increase the competitiveness of Australia's tax settings** – this is must be a first priority to keep Australia's business environment competitive against international standards
66. **Closing the gap between the company tax rate and the higher personal income tax rates**
67. **Abolish stamp duty** on business conveyances, as promised in the 1999 Intergovernmental Agreement on the reform of Commonwealth-State Financial Relations
68. A review of the costs/benefits of **reducing stamp duty on the sale of residential property** to first home buyers
69. **Eliminating the cumulative impact of the Goods and Services Tax (GST).** Specifically, stamp duty should be levied on the GST exclusive price of property and land. Not doing so is imposing 'a tax on a tax'.
70. Reforming developer (infrastructure) charges through the offer of **competition payments that compensate State and local governments** and councils for implementing policy that reduces the tax burden on new residential developments.

7.1 Australia's tax system is not producing the same amount of revenue for the same amount of tax as it used to. Conversely, the community is seeking increased services from government. But the increasing ease that capital (and investment) can cross borders means the tax system must also be internationally competitive. The answer does not lie in more and increased taxation.

7.2 Meanwhile, the economy is also not providing the windfall it once did. As much as the mining boom was a win for the economy, it was an even bigger win for the Budget. Company taxes ballooned, while investment into expanding mining / oil and gas infrastructure pushed up everything from retail spending to house prices.

7.3 Australia cannot rely on the world to underpin the nation's taxation challenge. Tax reform must be the fundamental response to put Australia back in a competitive position. As a net importer of capital our 30 per cent company tax rate provides a direct disincentive for businesses to make investments in Australia – for international and Australian companies alike.

7.4 The building and construction industry relies, in large part, on imported foreign capital to fund major infrastructure project and residential construction activity. Reducing the company tax rate to 25 per cent, at a minimum, would help to restore Australia's competitiveness in a world where international capital is highly mobile and global corporate tax rates are have been falling for a number of years.

7.5 The building and construction sector is one of the most intensely taxed in Australia, and bears a direct and indirect tax burden from all levels of Government — Federal, State/Territory and local. This high and onerous tax burden distorts investment decisions, discourages entrepreneurship and innovation, and reduces business investment and employment opportunities. It also diverts scarce resources into unproductive and unnecessarily costly -time and money -tax compliance within a key sector of the Australian economy.

Master Builders Tax Reform Agenda

7.6 Master Builder's tax reform priorities are expressed in a number of detailed submissions to the Government including as part of our *Strong Building Strong Economy* 2016 pre-election campaign, as well as in response to calls for input into the Submission to the Treasury's Affordable Housing Working Group (2016), the "Re: Think: Tax Discussion Paper" (2015), and previously in response to the finding of the Henry Tax Review (2010). Our tax reform priorities remain largely unchanged given the lack of implemented policy changes to come out of the Governments White Paper and subsequent discussion papers.

7.7 There has been a considerable body of work undertaken by Treasury, the Productivity Commission and other entities that have identified the areas of taxation in need of reform if we are to remain globally competitive. The challenge is for Government to begin the complex process of implementing the raft of reform recommendations of previous reviews and Papers.

7.8 Master Builder's main priorities for tax reform for the building and construction industry are:

- To provide incentive payments (competition payments) to encourage reform of state/territory land and property tax policies to reduce the unfair tax burden placed on the property sector, as well as the removal of planning and zoning impediments to the efficient supply of new homes.

- Retaining the tax exempt status of home ownership and to keep negative gearing rules intact..

- Reducing the company tax rate to 25 per cent for businesses of all sizes

- To simplify tax compliance and reduce repetition of red tape across different levels of Government.

- To reduce the difference between the highest income tax bracket and the company tax rate.

- A review of the scope of the GST to be broader based, to help remove the structural deficit in state/territory and the Commonwealth Budget, and a review of the potential to use higher GST revenues as an offset to reduce state/territory Governments reliance on property taxes and stamp duties.

- To remove taxes that are unfair or constitute 'double taxation'. For example, GST imposed on stamp duty is unacceptable. It is a tax on a tax. Future tax reforms must also be considered in the same way and should not be implemented if there is a possibility of 'double taxation'.

- Any changes to tax concessions that incentivise savings should be consider very carefully, particularly in the housing market.

7.9 Australia's tax system must be as efficient and globally competitive if Australia is to fulfil its economic potential and remain an attractive destination for globally sourced investment and capital. This is an important underpinning to sustaining and advancing our standard of living.

Competition payments

7.10 Master Builders supports Recommendation 48 of the Harper Review into Competition Policy that notes the use of competition payments and the establishment of the Australian Council for Competition Policy to provide incentives for state/territory and local Government reforms.

7.11 Competition payments have worked before, as part of the National Competition Policy (NCP) reform program that followed recommendations from the 1992 Hilmer Review – competition payments would work again.

Company Tax

7.12 Private business investment levels, it would appear, are not responding to record low interest rates. Businesses need incentives and certainty to grow and employ more workers, which in turn, will support employment and wage growth.

7.13 Australia's company tax rate is too high, it is a barrier to Australia's economic competitiveness and is a disincentive for foreign investment. As a net importer of capital it is important that Australia's tax system supports the flow of international capital into the Australian economy.

7.14 Australia's company tax rate is uncompetitive compared to an OECD average of 24.81 per cent (2015). Reducing the company tax rate to 25 per cent for businesses of all sizes is not a tax grab for businesses, it is a sensible response to the increasing international mobility of capital, at a time when other countries are reducing their corporate tax rates.

7.15 Master Builder recommends reducing the company tax rate to 25 per cent for all businesses by the end of decade. The goal must be for Australia's company tax rate to be globally competitive by 2030.

7.16 Company tax is an inefficient tax. The US and UK recognise this and have made public commitments to significantly reduce their tax rates, following the path of many countries before them who have much lower company tax rates than Australia.

7.17 Master Builders also calls for a reduction in the differential between the higher marginal personal income tax rates and the company tax rate. Such a measure would help improve tax compliance and, through lower income tax rates, improve productivity and workforce participation (especially by secondary and marginal earners) and act as an incentive for domestic saving which would, in turn, lower the cost of capital for business, especially smaller businesses.

Goods and Services Tax

7.18 Master Builders recommends the Government reconsider the potential for the GST to be broader based despite the political challenges. This could be achieved by independent external reviews for instance. The clear benefit will be the increase in revenue to assist in the rebalancing the structural Budget deficits across State/Territory and Commonwealth Governments and would be in line with Recommendation 51 under section C2 of the Henry Tax Review (2009). The broadening the GST base, would help offset proposed reforms to state/territory property taxes and charges.

7.19 Master Builders Australia recommends that the cumulative influence of GST be removed. In particular, GST imposed on stamp duty is unacceptable. It is a tax on tax. If stamp duty must be charged then it should be calculated on the GST excluded price.

8 Housing Affordability

More homes, fewer taxes, quicker approvals and less red-tape are essential elements to keep homeownership within reach of everyday Australians

Policy Recommendations:

71. Introduce **payments to higher-performing local governments** based on national competition policy principles, with the aim of encouraging improved delivery of housing related services, amenities and infrastructure.
72. **Streamlined and simplified development approvals** processes for residential developments, with a greater reliance on a code-based assessment and identification of best practice development approvals processes in state/territory and local government.
73. State/territory and local governments to develop and implement **tailored Land Release Plans**. This would include identifying ways to overcome regulatory or other impediments to the supply of new land zoned for residential development.
74. Creating a genuine, comprehensive and enforceable **uniform building code and regulatory system**. COAG must play a leading role in developing the BCA into a nationally consistent central authority for building and construction across all jurisdictions.
75. Ensuring state/territory governments honour their commitment to **abolish stamp duties** on business conveyance of real property.
76. **Develop and annual publication of developer charges applied by all local governments in Australia**. This would not leave anywhere for overcharging local governments to hide and would increase the transparency between infrastructure charges and infrastructure costs.
77. **Improve access to affordable housing**, through increased funding and alternative funding models and better collaboration across the different levels of government and the private sector

8.1 Master Builders welcomes the clear recognition by the Federal Government of the ongoing problem of housing affordability across all Australian capital cities, and a growing number of regional growth areas. The White Paper on Taxation (Henry Review, 2009), the subsequent Treasury discussion papers “Re;Think: Tax Discussion Paper”, the Senate Inquiry into housing affordability, the House of Representatives Standing Committee “Report on the Inquiry into Home Ownership”, and the Treasury inquiry into innovative financing models for affordable/social housing, provide important opportunities for action on reforming inefficient taxes and charges, and to reform the structural barriers which unnecessarily inflate the cost of housing and limit new housing supply.

“Measures to increase land supply… would likely stimulate an increase in production and a reduction in the price of new housing.” (National Housing Supply Council Report, State of Supply, 2009)

8.2 Master Builders calls on the Federal Government work through COAG to address the numerous bottlenecks and impediments to supply in the residential building sector. The Federal Government must provide leadership to work with State, Territory and local jurisdictions to remove unnecessary supply constraints and abolish or reduce inefficient property taxes and charges.

8.3 The adequate supply of appropriate and affordable housing is a critical part of the Australian economic and social fabric. Australia has one of the highest rates of home-ownership in the world but this is slipping. More than two-thirds of Australians currently own or are in the process of buying their own home. The high rate of home ownership and strong public policy commitment over many years by Governments of both major political persuasions to home ownership has enriched Australia both in economic and social terms. This must remain a key policy objective for all Governments - to ensure affordable housing is available for all Australians.

8.4 A co-ordinated and proactive public policy agenda by Federal, State and Territory, and local Governments is needed to facilitate home ownership and to reverse the trend which is seeing homeownership increasingly being out of reach of a growing share of the Australian population. The cost of a family home has increasingly become unattainable as a confluence of circumstances has worked against would be Australian homeowners, particularly first home buyers.

8.5 Key factors that have led to a worsening of housing affordability include:

- shortage of available land and inefficient land release strategies;
- infrastructure costs being loaded onto developers and in turn passed on to home owners;

- excessive infrastructure specifications in subdivisions;
- excessive development levies, taxes and charges imposed by State and Territory Governments;
- excessive planning and building requirements;
- regulatory creep pushing codes and standards higher than required; and,
- uncoordinated State/Territory and local Government environmental regulations.

8.6 Master Builders calls on the Federal Government, through a reinvigorated COAG, to provide ex poste 'competitive, efficiency dividend' payments to State, Territory and local Governments for delivering housing affordability policy outcomes against key performance metrics. Master Builder's position is consistent with Recommendation 48 – competition payments, of the Australian Government's Competition White Paper (Harper Review, 2015)[1].

8.7 Key elements of a robust National Housing Affordability Agenda (NHAA), and associated 'competitive, efficiency dividend' payments, include:

- Tangible outcomes in improving the efficiency, and the supply-side efficiency in particular, of the Australian housing market;
- Annual publication by the Federal Department of Industry on its website of a rigorous and transparent stocktake of approaches to developer/infrastructure charges by all local Governments in Australia. The stocktake would examine the nature, the processes involved and the incidence of the charges imposed on 'brownfields' and 'greenfields' (both fringe and infill) developments for a normalised set of developments;
- An efficient housing market, which would have a number of features, including one not burdened by unnecessary distortions: (to make market prices the principal method by which housing demand signals are transmitted to housing

[1] Detailed policy description is found under section 8.8 – 8.12 in later sections of this submission.

suppliers); and, by regulatory, and poorly targeted subsidy and taxation intervention;

- Streamlined and simplified development approvals processes. Achieved through greater reliance on code-based assessment, identification of best practice development approval procedures amongst State, Territory and local Governments, as well as expanded use of performance monitoring and benchmarking;
- Local Governments to develop and circulate individual, realisable Land Release Plans for their own jurisdictions over a ten year rolling time horizon. These Plans would identify specific tracts of land within own-jurisdictions, set down timelines for their prospective availability for residential development, any regulatory or other requirements which may impede the land release process, generally and for specific tracts of land, and nominate those tracts which would be 'development-ready' within five years.
- The realisation of a genuine, rigorous, enforceable and uniform building code and regulatory system to ensure the development and continuation of an efficient and competitive building industry. The COAG members should also continue to play an active leadership role in the ongoing development and refinement of the NCC as the central document specifying a national set of building requirements; and,
- Ensuring the State and Territory Governments honour an existing, long overdue commitment to abolish stamp duties on business conveyances of real property. This would be followed by a rigorous review of the impact of stamp duty on residential property, and alternate approaches to revenue-raising.

8.8 In the medium to long term, committing to a NHAA by removing or ameliorating structural legislative, regulatory and fiscal impediments to housing supply will result in less outlays in transfers and in the provision of public and social housing, and less upward pressure on inflation. In other words, there is a structural dividend to be gained.

8.9 The housing supply issue has not been resolved. The two key recommendations flowing from the Henry Review's analysis of Australia's housing affordability challenge — free up zoning and planning; and set appropriate infrastructure charges (developer charges) must be top priorities for the Federal Government.

8.10 In the taxation sphere, Master Builders advocates urgent reform of inefficient and costly infrastructure taxes, charges and levies.

8.11 Master Builders housing policy also advocates:

- maintaining the tax-exempt status of the family home;
- retaining the current negative gearing provisions;
- provision of an appropriate level of public housing, starting with decisive action to provide suitable accommodation for the more than 43,000 persons, assessed as being in greatest need, on public housing waiting lists. This equates to unmet demand for over 16,500 public housing dwellings; and,
- mandatory minimum energy efficiency standards not to exceed six stars.

Negative gearing

8.12 Master Builders urges the Government to maintain its policy to keep negative gearing rules for property investment unchanged and intact. Removing negative gearing rules from property investment, but not other types of investments would constitute unfair treatment of property investors and cause a greater variation in the treatment of debt financed versus equity finance.

8.13 Keeping negative gearing on property investments would ensure capital investment into property is treated equitably compared to other types of capital investments like stock, or investment into capital used in the generation of personal income, such as tools for trade workers.

8.14 The Australian Taxation Office (ATO, 2016) reports almost 1.3 million personal income taxpayers claimed net negative rental income on residential property of almost $3.8 billion (or an average of just over $2,920 per claimant) in the 2013/14 financial year (the latest for which figures are available).

8.15 The taxation treatment of investment properties (which includes negative gearing) has been given expansive consideration in recent reviews (both completed and ongoing) of Australia's taxation system, most notably:

- the "Australia's Future Tax System" review (also known as the "Henry Report; Australian Government (2009); and,
- the current "RE: Think" tax reform process (Australian Government, 2015).

8.16 In short, both reviews cautioned against changing the tax treatment of investment properties, particular before structural impediments to supply are addressed and resolved.

8.17 The "Henry Report" (Australian Government, 2009) in their final report concluded (page 418):

- changing the taxation of investment properties could have an adverse impact in the short to medium term on the housing market; and,
- changes to the tax treatment of investment property should only be adopted following reforms to the supply of housing (for example, land release policies).

8.18 Taken as a whole, the Henry Report concluded (at page 420):

> *"A range of other policies are likely to have a more significant impact on housing supply than tax settings.*
>
> *The tax system is unlikely to be an effective instrument to move housing prices toward a particular desired level and the tax system is not the appropriate tool for addressing the impact of other policies on housing affordability."*

8.19 The Government's tax reform process (Australian Government, 2015) also makes a number of important observations (at pages 63 to 65 inclusive) about the operation of 'negative gearing' within the Australian taxation system.

8.20 These observations include:

- the tax treatment of investment in real estate is the same as that for investment in any other asset which produces current incomes;
- many of the reasons people invest in residential property rather than other assets have little to do with taxation;
- negative gearing of itself does not cause a tax distortion;
- negative gearing allows more people to enter the asset market (for example, residential property) than would otherwise be the case (for example, if they relied on equity funding alone);
- negative gearing promotes consistency of treatment between debt and equity funding (through its treatment of interest expenses); and,
- any taxation advantages for individuals investing in residential property do not come from borrowing (that is, negative gearing) but rather from the tax treatment of any capital gains on the asset concerned.

8.21 The House of Representatives Standing Committee on Economics, "Report on the Inquiry into Home Ownership" (2016) made a number of important observations that further support negative gearing as part of the tax system:

- Negative gearing is not a tax deduction accessed primarily by the rich. Indeed the Treasury, in its, "Re:Think – Tax Discussion Paper" notes that "the distribution of people with negatively geared properties follows that of the tax system, that is, the majority are in the middle income bracket." Master Builders has done extensive work into the profile of housing investors and would be willing to talk further with the Treasury in regard to the matter.
- The Reserve Bank commented, "in terms of our financial stability mandate, we think that it is within our mandate to make observations about where in the institutional framework, including the tax system, there might be incentives to engage in more leverage, because it is the leverage piece that is so important for financial stability, both of the financial sector and of the household sector."

8.22 In this context, changing or removing negative gearing rules from property investments, presents a greater risk to Australia's financial stability and the stability of the housing market. Master Builders sees this as an unacceptable risk to the Australian economy and Australian living standards given the housing sector is home to over two-thirds of the asset portfolio and wealth of ordinary Australians.

8.23 By promoting private investment into property, negative gearing helps to reduce Government expenditure on social and public housing. Modelling by Master Builders estimates that negative gearing accounts for between 9 and 11 per cent of the supply of new rental properties each year.

- In 2014-15 this equated to more than 22,900 new dwellings, providing shelter for over 60,800 people.
- The counterfactual, had negative gearing not been available, would have meant Governments, at the state and federal level would have been called upon to fund the supply of these homes, at a cost of over $16 billion.

8.24 Master Builders rejects claims from some commentators and the opposition that removing negative gearing would constitute a budget saving, due to the offsetting additional demand for social and public housing that would need to be funded. In 2014-15, net negative gearing payments cost $3.72 billion, far less than the cost of supplying additional social and public housing.

8.25 In terms of the economy, treating one form of investment different to others can have long-term consequences for the efficient allocation of capital, and long term productivity. Policy must not encourage one form of investment over others.

9 Small Business

Small business is a crucial part of the building industry, the economy and our country. More small businesses and less regulation are essential ingredients for our future prosperity

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Policy Recommendations:

78. Delivery a **small business-friendly environment** and boosting confidence through stable economic settings.
79. **Security of payments for subcontractors** through policy that protects subcontractors from taking on the implicit business risks of their larger contracting counterparts.
80. Targeted measures to **assist small business employers to take on more apprentices** and help to increase the completion rates for building trade apprentices.
81. **Streamlining the development approvals processes** to help smaller business stem the growing shortfall in new housing supply.
82. **Simplified tender processes and reduced costs** to encourage more small businesses participation in government funded building and construction projects.
83. **Reviewing current regulation at all levels of government** in terms of their real economic cost, with the aim of removing inefficient regulations that bare a high economic cost – regulators should approach regulatory review and removal with the same level of vigour given to the implementation of new regulation.
84. **Subject all new regulations to a transparent and rigorous cost-benefit** analysis framework that is endorsed by the Productivity Commission and is subject to public scrutiny.
85. **Simplify business tax compliance**, recognising that inefficient collection and administration of taxes distorts economic decision making and capital investment.
86. **Assist small businesses by reducing the broader complexity of taxation and industrial relations laws**, tackle the compliance costs of regulation - which too often form an indirect competitive disadvantage for small businesses compared to large businesses – increase their ability to access debt and equity finance and do more to facilitate their participation in government procurement.

9.1 Small businesses account for nearly 98 per cent of firms in the building and construction industry. These 344,000 small businesses are a key engine of productivity in the building and construction industry.

9.2 Without a confident, energetic, entrepreneurial and innovative small business sector, we cannot have a strong building and construction industry, a strong economy, more liveable communities, strong employment growth, and more training opportunities.

9.3 The building and construction industry is one of the most intensely regulated industries in Australia, with legislation and regulation imposed at all three levels of Government.

9.4 Unnecessary over-regulation shackles the industry with ‘red’ and ‘green’ tape, sapping entrepreneurial effort and stunting innovation and productivity growth. It stops small business from doing what it does best – creating jobs.

9.5 Master Builders welcomes the Government’s intention to reduce the regulatory burden through an aggressive agenda to cut $1 billion in red and green tape, and would encourage the Government to focus on removing regulations that limits the construction of new homes, hospitals, schools and roads.

9.6 New regulation must be test rigorously against a standard cost-benefit analysis, endorsed by the Productivity Commission and made available for public scrutiny.

Business simplification

9.7 Master Builders welcomes moves by the Federal Government to cut company tax, reduce medium term spending and privatise assets, as this should over time free up resources and assist individuals and businesses to succeed. Also welcome are moves to reduce the regulatory burden on business, individuals and the community by $1 billion a year through an aggressive agenda to cut red and green tape.

9.8 Master Builders supports the Governments Business Simplification Agenda and would support additional funding into the program to undertake research into the performance of local Governments and Government agencies and programs.

10 Workplace programs/agencies

The building industry needs a safe and productive workplace relations environment

Policy recommendations:

87. **Proper resourcing for the Australian Building and Construction Commission (ABCC)** to properly fulfil its increased mandate to; increase productivity, reduce disputes and delays, foster greater cooperation between workers and employers on commercial building sites and the economy in general
88. **To keep the remit of the ABCC to that outlined above**. **Issues pertaining of 457 visa's** and visa holders, as well as the scope of their application should be left to the appropriate government department and **should not form part of the remit of the ABCC**
89. **Preserve the rights of independent contractors** by retaining the current laws that give people choice about how they work and encourage entrepreneurship
90. **Ensure the Registered Organisations Commission (ROC) is properly funded** and focused on ensuring building union officials are held to a standard that is consistent with those expected from our business leaders and elected officials
91. Adopt **a workplace bargaining system in which employers and employees can freely enter into appropriate and lawful workplace agreements**, underpinned by simple safety net conditions. Employers and employees must be the two most important parts of an employment relationship. **The role of third parties should only exist where invited** and must never take precedence over the wishes of employees or employers
92. **Implement fair and simple dismissal laws that place more emphasis on the right of employers** to manage their own business, reflect community expectations and embrace the notion of 'common sense'
93. Continue to pursue **nationally consistent workplace safety laws** and increase the focus on practical safety outcomes and a safety orientated workplace culture
94. **Stop and reverse the growth in overlap between safety laws and industrial relations laws**
95. **Ensure that the concept of workplace safety is not further sullied** by prohibiting notions of 'safety' from being exploited as a tactic to achieve industrial relations outcomes
96. **Review the operation and work of Safe Work Australia** to reduce duplication with other bodies, focus operational activity and improve engagement with employers, including through the appointment of more business representatives to its board

97. Master Builders supports the **Harper Review recommendation (Recommendation 36) on the prohibition of secondary boycotts** in sections 45D-45E of the *Competition and Consumer Act (2010)* to be maintained.

10.1 The building and construction industry places a high priority on a safe and productive workplace relations environment. Harmonious, safe and productive workplaces are vital for a strong building industry, a thriving economy and more job opportunities for all Australians.

10.2 We need 300,000 more workers, independent contractors and apprentices over the next decade, however current workplace laws discourage many from hiring more workers and training more apprentices.

10.3 The building and construction industry is committed to delivering safe and productive workplaces for the more than one million people it employs. The personal and community cost of serious injury and death at work cannot be underestimated and must be addressed.

10.4 Safer and more productive workplaces can be achieved without adding to the existing level of complexity and compliance. A common sense, practical approach is needed.

10.5 The focus must be on the quality, rather than the quantity, of legislation and regulation. The focus must also be on education and awareness, injury prevention, and the practical and achievable management of foreseeable risk, not just paper based compliance. It's about creating a genuine 'safety culture' in the workplace.

10.6 To address these challenges Australia must return to a balanced and fair industrial relations system. It must be easily understood and simple.

10.7 The building and construction industry unions have a long history of militant and unlawful behaviour, such as unlawful strikes and other illegal activities, which disrupts workplaces, stifles productivity and adds up to 30% to the cost of building community facilities such as hospitals and schools – an impost funded by taxpayers.

10.8 The Australian Building and Construction Commission (ABCC) must be appropriately resourced to increase productivity, reduce disputes and delays, foster greater cooperation between workers and employers on commercial building sites and the economy in general.

The Importance of the Building and Construction Workplaces to Government Consideration

10.9 The building and construction industry is the second largest industry in the economy and employs a workforce that totals almost 1.1 million in number. Government decisions as to workplace policy, programme, agencies and regulation are almost all likely to have a significant impact on, and implications for, workplaces in the building and construction industry.

10.10 As an industry experiencing a trend of positive growth, the current and future needs of the building and construction workplaces should be a central consideration to Government as it considers policy and funding matters, such as those noted elsewhere in this submission about skills and future labour requirements.

10.11 In terms of contemporary considerations and immediate issues, the sector is renowned for its ongoing extensive and high-profile involvement in workplace related matters. For example:

- Approximately one third of the Final Report of the Heydon Royal Commission was devoted to the building and construction sector and comprised of two distinct specific volumes. This was yet a further inquiry following the Cole Royal Commission and the Gyles Royal Commission, in addition to a significant number of other sector specific inquiries, reviews and reports.

- Australian Bureau of Statistics (ABS) data shows a trend towards increasing levels of workplace disputation and days lost to industrial disputes. The most recent data showed the construction industry lost 14,500 days to industrial dispute in the September quarter 2016, accounting for 42% of total days lost (34,900) across all industries. Over the year-to September 2016 the number of days lost to industrial disputes in the building and construction industry has jumped by over 102 per cent.

- The predecessor to the Australian Building and Construction Commission (ABCC) known as Fair Work Building Construction (FWBC) commenced 32 new proceedings for breaches of the law involving Adverse Action (seven proceedings) Unlawful Industrial Action (six proceedings) Coercive Behaviour (fourteen proceedings) and Right of Entry (five proceedings) during 2016.

- Building and Construction industry unions have been fined a total of approximately $1.8 million since June 2015 for breaches of industrial laws, with over 100 building union officials currently before the courts facing over 1000 separate charges.

- The sector has been identified as a 'priority industry' by Safe Work Australia given its high number and rates of injury and/or fatalities, therefore leading it to being considered hazardous by nature.

10.12 The above issues merely scratch the surface of available indicators that represent demonstrable evidence of the important relationship between workplaces in the building and construction industry and Government policy.

Master Builder’s Workplace Policy Priorities

10.13 The most important policy priorities maintained by Master Builders Australia are:

- Ensuring respect for the rule of law in the building and construction industry by ensuring the Australian Building and Construction Commission (ABCC) is sufficiently resourced;

- Preserve the rights of independent contractors by retaining the current laws to give people choice about how they work and encourage entrepreneurship;

- Supporting the Registered Organisations Commission (ROC) to ensure building unions are accountable to members and their officials act like everyday people;

- Adopt a workplace bargaining system in which employers and employees can freely enter into appropriate and lawful workplace agreements, underpinned by simple safety net conditions;
- Ensure all workplace laws respect that employers and employees are the two most important parts of an employment relationship. The role of third parties should only exist where necessary or invited, and must never take precedence over the wishes of employees and employers;
- Implement fair and simple dismissal laws that place more emphasis on the right of employers to manage their own business, reflect community expectations and embrace the notion of 'common sense';
- Continue to pursue nationally consistent workplace safety laws and increase the focus on practical safety outcomes where a safety-oriented workplace culture and individual responsibility takes precedence over, and is considered as more important, than paper-based compliance;
- Stop and reverse the growth in overlap between safety laws and industrial relations laws, to improve compliance, and reduce complexity and confusion;
- Ensure that the concept of workplace safety is not further sullied by prohibiting notions of 'safety' from being exploited as a tactic to achieve industrial relations outcomes.

10.14 The above priorities are canvassed in further detail hereunder in addition to other policy matters.

Responding to the Inquiry Recommendations – the Productivity Commission's Report into the Workplace Relations Framework (PC Review) and the Royal Commission into Trade Union Governance and Corruption (Heydon Royal Commission)

10.15 Master Builders emphatically supported the initiation of these two reviews. The PC Review was handed down on 21 December 2015 and the Heydon Royal Commission final report on 30 December 2015.

10.16 To date, there has been no detailed Government position in response to the majority of recommendations arising from same and we would encourage Government to determine and announce a position in the interests of industry certainty.

10.17 This is particularly important to the BCI as both reports contained recommendations that had specific application to the sector.

Change to the Fair Work Act – General

10.18 Master Builders has maintained a consistent and evidence based policy position with respect to necessary changes to improve the operation of the Fair Work regime.

10.19 To avoid repetition of those positions in detail, we set our hereunder a summary of the central elements of necessary reform.

10.20 **Enterprise bargaining** is stated to be 'the heart of the workplace relations system' introduced by the FW Act. However, based on the experience of building industry employers it has failed to properly balance the interests of employers against those of employees and unions. At the centrepiece of the FW Act's enterprise agreement regime are the principles of 'good faith bargaining'. Yet it is clear that protected industrial action is able to be taken prior to discussions for an enterprise agreement having taken place. This 'strike first talk later' position is clearly at odds with the intention of enacting 'clear, tough rules' about industrial action under the FW Act and significantly undermines the intended good faith bargaining regime and hampers productivity by providing an industrial weapon to militant unions such as those which operate in the building and construction industry.

10.21 Master Builders is also concerned about the **scope of permitted content in enterprise agreements**. This subject area affects the ability of employers under the FW Act to appropriately regulate business-to-business contracts between an employer and independent contractors, as these relations are able to be adversely affected by unions under terms set out in pattern union enterprise agreements. This significantly impedes productivity within the building and construction industry, where the use of specialist contract labour is essential to the viability of construction projects. These trends represent significant alterations in the balance between employers, employees and unions.

10.22 Agreement **clauses which restrict the use of contractors and labour hire** are having a negative effect on the industry, particularly its costs. Master Builders' position is that regulation of independent contractors through enterprise agreements should be treated as an unlawful term per s194 of the FW Act. This position would ensure that costly litigation about this issue and the effective regulation of contractor terms and conditions by unions via this inappropriate mechanism were outlawed. In the building and construction industry in particular, this step would have no adverse effects on job security as the provision that is pushed by unions is effectively a measure to ensure that competitive wages and conditions cannot be introduced; job security is the guise under which unions become the gatekeepers of terms and conditions on site.

10.23 **Transfer of Business** rules under the FW Act are dense and difficult to apply. This particular part of the legislation has proved disappointing as it overturned the long established and well understood laws regarding transmission of business and was not contained in the Labor Party's Forward with Fairness policy framework which formed the policy basis of the legislation when first formulated. The pre-existing laws operated on the simple premise that a person could not transfer a business and thereby avoid their industrial obligations. The FW Act has expanded the reach of these laws to circumstances where it cannot reasonably be said that a business has actually been transferred. Moreover, it creates a framework that delivers absurd outcomes and which are unfair to employers and which have restricted opportunities for employees. Previous transmission of business rules, based on the actual transfer of a business, must be reinstated.

10.24 The **unfair dismissal laws** under the FW Act have failed to deliver a fair outcome for employers. There is growing anecdotal evidence that the objectives of the FW Act in relation to unfair dismissals remain purely aspirational, and the needs of business are not being met. The procedures for dealing with unfair dismissal are neither quick, nor flexible, nor informal.

Compliance is not easy for business. Employers are forced to spend time and money defending often speculative claims, with the vast majority being resolved through commercial settlements. It remains a jurisdiction of "go away" money, where reinstatement remains impracticable.

10.25 The FW Act has failed to provide fundamental protection for **small business employers**, with the legislative balance clearly favouring employees. The lack of such protection is damaging Australia's resilience in the face of the uncertainty and instability in local and international economies.

10.26 The small business exemption from unfair dismissal that currently exists is unlike earlier versions, which gave a complete exemption by eliminating any unfair dismissal remedy under the relevant legislation for any employees of the small business. The difference is very significant as the current exemption law still exposes the small business to the high standards of procedural and substantive requirements. After the first 12 months of service of an employee, a dismissal by a small business employer can be challenged on both substantive fairness and procedural grounds. The consequences can be long mediation and FWC procedures with uncertain outcomes, especially with regard to compensation. The dismissal might be declared invalid by the FWC and create uncertainties, particularly if reinstatement is ordered. This is unreasonable. The additional costs and resources expended by a typical small business to introduce advanced employee management systems and to contest potential claims of unfair dismissal have been acknowledged by every Government since 1982. Notwithstanding this prior consideration the current termination laws are the least supportive of small business in 35 years.

10.27 Master Builders supports the reintroduction of a true 'exemption', where a remedy for alleged unfair dismissal is unavailable to employees of small business. The law must also be recalibrated so as to place more emphasis on the **employer's prerogative to manage** their business. Laws defining a valid reason for **redundancy** should be confined to termination for reasons based on the operational requirements of the employer's business.

10.28 Master Builders considers that the **adverse action** provisions of the FW Act should be abolished. Alternatively, if they are to be retained, they must be rebalanced in order to avoid potential scope for abuse. At the least, the 'sole or dominant reason' test should be reinstated.

10.29 There has been a significant widening of both “workplace rights” and “lawful industrial activities” under the FW Act compared to earlier federal workplace relations laws. Master Builders considers that the adverse action provisions of the FW Act provide an unnecessary layer of additional and excessive remedies to employees, who are already protected from unlawful or unfair termination and discrimination under other laws.

10.30 The **reverse onus of proof** and the removal of the “sole or dominant reason” exemption raise significant issues for employers. Add to this uncapped compensation available in adverse action remedies, as well as none of the unfair dismissal jurisdictional exemptions, the employee’s preference towards bringing adverse action claims in the Federal Court rather than unfair dismissal applications in the FWC is obvious. This trend significantly compromises the positive policy outcomes in having a workplace relations tribunal with an emphasis on being quick, informal and avoiding unnecessary technicality.

10.31 Laws regulating **industrial action** must balance the rights of employees to seek improved terms and conditions with the importance of acting lawfully, in good faith. At the same time productivity must be maximised. The FW Act does not deliver the correct balance. The FW Act should be amended to make it clear that parties must be acting in good faith in order to take protected industrial action.

10.32 Protected action ballot orders must consider **pattern bargaining.** Pattern bargaining has been a blight on the building and construction industry, a drag on productivity and detracts from value-for-money in Government and private procurement. Pattern bargaining leads to poor outcomes for all concerned, particularly in relation to the loss of value-for-money in public works. The results of pattern bargaining have been detrimental to both workers and employers, to the industry and to the national economy.

10.33 The FW Act does not contain a requirement that a party must satisfy the Commission that it is not pattern bargaining before applying for a protected action ballot. This, combined with the absence of any constraints relating to good faith bargaining, have permitted the re-establishment of ‘take it or else’ agreement making.

10.34 **Right of entry** (RoE) provisions under the FW Act urgently need attention. There is ample evidence to suggest that the current obligations concerning RoE rules are being abused, and there is no recourse against union officials who intentionally fail to renew entry permits. A number of CFMEU officials have, for some time, adopted the practice of letting their permits lapse to avoid action being taken against them. Contractors are then faced with the escalation of a dispute which invariably requires police involvement to remove union officials on the grounds of trespass.

10.35 The current laws are also failing the industry because union officials are provided with a discretion to either show, or not show, their federal permit. The law must be amended to mandate the production of entry permits if union officials wish to exercise legitimate right of entry privileges.

10.36 If RoE abuses are to be adequately addressed in the building and construction industry, real, substantial and certain penalties must apply. Union officials should know that if they abuse the rights and privileges attaching to a permit, their permit will be suspended for a minimum known period or revoked entirely.

10.37 The subject of **sham contracting** is an important matter to the sector. A sham contract arrangement arises when an employer deliberately treats an employee as an independent contractor or coerces employees into signing contracts that represent them as being contractors rather than employees. This is currently proscribed in s357 to s359 FW Act. Master Builders stresses that this behaviour is a deliberate act by those who choose to act illegitimately. It is a practice we condemn. It should not, however, be confused with misclassifying an employee as a contractor, a mistake that may often be made because of the dense and confusing law that governs this distinction, inclusive of a multitude of statutory deeming provisions.

10.38 The attempts to paint sham contracting as something different to the deliberate manipulation of the law promotes a range of other agendas. Firstly, it assumes that sham contracting is an endemic problem in the building and construction industry or other industries. This is not the case. Secondly, it enables unions where members are employees rather than a contractor to discourage the formation of independent businesses as a means to boost membership.

10.39 Much of the agenda of those who seek to oppose the current law is based upon making misclassification akin to sham contracting. This is lamentable given the state of the complex law which distinguishes between whether a worker is an employee or a contractor. Employers can already suffer very problematic financial burdens following misclassification if they are then asked to reverse the status of a worker. Adverse cost consequence should not be added to by labelling misclassification an offence. The current provisions in the law should not be changed.

The Fair Work Commission (FWC)

10.40 In accordance with s.156 of the Fair Work Act, the FWC is required to conduct a **4 yearly review of modern awards**. Master Builders is heavily engaged in the review, with an interest in both the *Building and Construction General On-Site Award 2010* and the *Joinery and Building Trades Award 2010* (Construction Awards). We are also a party to a number of 'common issue' award matters relevant to the building and construction industry.

10.41 The FWC devotes a substantial amount of resources to the 4 yearly review process, which also poses a significant drain and unreasonable burden on the parties required to participate in the various review proceedings.

10.42 The review process is flawed on a number of additional levels which was highlighted in the PC's report into the Workplace Relations framework. First, although the current review commenced in 2014, the FWC has yet to conduct any substantive hearings (let alone hand down a decision) in the Construction Award matters. Second, the process also requires the giving of evidence, which in our sector can be difficult to garner in light of the reluctance of third parties to make statements for fear of reprisals from unions. Third, the position of the parties to the review process is often polarising giving rise to an adversarial process that does little to genuinely address gaps or anomalies within modern awards.

10.43 Master Builders is of the view that the **4 yearly review should be abolished** and **replaced with a regime that provides for parties to make applications to have specific provisions within modern awards reviewed on a merit basis** as the need arises. This would significantly reduce the amount of resources, both on the part of the parties and the FWC, required to facilitate the 4 yearly review process.

10.44 Master Builders also has great concerns about the FWC's **processes associated with the approval of enterprise agreements**. Currently when an agreement is lodged for approval it is uploaded to the FWC's website where any visitor to the relevant page can view the document in its draft form. This process provides union non-parties to enterprise agreements with the opportunity to frustrate the approval process if they so desire, for example if the proposed agreement is inconsistent with a 'union pattern agreement', even if the proposed agreement does not cover a union member.

10.45 This practice has an adverse effect on employers, particularly small to medium sized businesses that make up the overwhelming majority of Master Builders' membership. Unwarranted interventions by unions to the approval process has had the effect of causing significant delays in agreements being approved and in some cases significant costs to employers who are then forced to engage representatives to represent their interests.

Australian Building and Construction Commission (ABCC)

10.46 Master Builders welcomed the re-establishment of the ABCC as a specific industrial relations regulator for the building and construction industry. The ABCC worked when it previously existed and the sector has confidence that it will do so again. Combined with the establishment of a Registered Organisations Commission (ROC), Master Builders envisages a marked improvement in sector workplace relations and the conduct of associated representative organisations.

10.47 The ABCC is expected to deliver significant benefits not only to the Australian building and construction sector but the community as a whole. Master Builders had estimated that the absence of the ABCC meant that the cost of construction in Australia was 30% higher than it ought to have been. Given the restoration of the ABCC and the estimated infrastructure spend of State and Commonwealth Governments combined forecasts for the next 10 years, the ABCC should generate a significant saving to Governments of all levels to the benefit of the community generally.

10.48 While a re-established ABCC is a positive development, Master Builders remains concerned about the effect of, and implications arising from, a number of legislative amendments that changed the law from that as it was initially proposed. There are both policy and agency consequences arising from these changes detailed hereunder.

10.49 The ABCC now has an expanded remit and role to play in areas that are not conventionally associated with industrial relations law, do not pertain to the relationship between employers and employees, or were previously the responsibility of other regulators, agencies or jurisdictions.

10.50 These additional roles include:

- taking on the role previously held by the Fair Work Ombudsman (FWO) in relation to building and construction industry workplaces;
- ensuring compliance with, the monitoring of, security of payment laws that apply to building and construction industry participants;
- dealing with matters relating to commercial contracting and related commercial conduct within the building and construction sector;
- involvement in a proposed security of payment working group (in which Master Builders seeks to be formally engaged);
- greater regard to matters involving the Australian Competition Law; and
- taking a more active role in terms of sector work health and safety.

10.51 There is significant concern that the focus of, and resources available to, the ABCC will be less concerned with its primary role and function and instead diverted towards matters that are ancillary or secondary.

10.52 It is Master Builders' strong and primary view that the additional elements for which the ABCC was given responsibility should be reversed. This means that these additional responsibilities returned to the regulators who have historically and properly held the requisite responsibility.

10.53 For example, ensuring entitlement compliance for employee entitlements in the building and construction sector would be returned to the FWO, an agency that is responsible for this function in every other sector of the economy. There is no reason why the FWO could not easily resume this role and it is simply confusing and inefficient (to the industry, workers and other regulators) for this exception to exist.

10.54 Further, given its size, background, experience and history, is far more efficient and effective on a recovery per input basis than any other regulator and certainly more efficient than the ABCC.

10.55 Standards of commercial conduct in the building and construction sector is something over which the Commonwealth has little or no jurisdiction. Laws dealing with payments between industry participants are the responsibility of State and Territory Governments. It is not appropriate for a Commonwealth agency to enforce the laws that are determined by other jurisdictions.

10.56 Master Builders believe that the regulator of commercial laws applicable to the sector should be those that already exist and the states and territories are responsible for enforcing their own laws. The ABCC should have little or no role to play, other than a broad monitoring role where repeated breaches can be identified and notification made to the relevant state or territory regulator.

10.57 In the absence of those roles being returned to the agency where they should properly be located, it is incumbent upon the Commonwealth to ensure that the ABCC is appropriately funded and resourced. This will ensure the ABCC can maintain their core role of ensuring compliance with special industrial law specific to the building and construction sector and participants, as well having capacity and resources to appropriately undertake the new responsibilities that they have been given.

10.58 To this end, it is Master Builders' view that the agency should have a recurrent funding increase of not less than $5m per year or $20m over the forward estimates period. The offset for this additional allocations should come from the regulators with whom responsibility previously sat, such as the FWO, or from state and territory regulators whose workload ought to be commensurately reduced given the new ABCC role.

10.59 Master Builders also takes the view that there ought to be a number of changes to the legislation relating to the ABCC and underpinning its operation. In short, Master Builders, as a matter of principle, supported the ABCC legislation in the form as originally introduced and it should be restored to that form.

Safe Work Australia (SWA)

10.60 Master Builders notes that SWA has undergone a recent review recommendations arising therefrom have been put in place. Notwithstanding this, Master Builders takes the view that it is appropriate for the Government to consider an additional SWA review that is narrow in terms to include the following matters:

- Duplication and overlap with other existing agencies and their work, particularly with regard to policy setting functions;
- The view of other regulators such as Work Safe NSW, Work Safe ACT, etc in relation to SWA and its role, function and purpose;
- The processes undertaken within SWA to develop materials and policy positions;
- The nature of data produced by SWA, including statistical materials published regarding industry injury and fatality rates; and
- Whether or not there is scope for other agencies (for example OFSC and or the Asbestos Safety Eradication Agency) to also be part of the SWA entity.

10.61 Master Builders would seek that the Government also amended relevant regulations as necessary to grant Master Builders a position on the SWA Board. The existing members are limited to the Australian Industry Group (AiG), the Australian Chamber of Commerce and Industry (ACCI) and two equivalent union positions. The Government should consider whether or not this appropriately reflects and serves the Government's policy goals of ensuring workplaces are safe and hazards are minimised.

10.62 The membership of the SWA Board should extend to the top three industry sectors that are considered 'priority industries'. SWA has categorised certain industries in this manner that are involved in work or sectors that are deemed to be at a level of risk that exceeds the average. Given the building and construction industry employs around one in ten people and is the second largest industry in the Australian economy, Master Builders Australia should have a position on the SWA Board whilst it remains a priority industry along with representatives from other priority industries.

10.63 In the alternative, the Government should consider re-establishing the Technical Advisory Group (TAG) that has previously existed in SWA and other predecessor bodies. The TAG was a way in which SWA and policy makers could interact with industry representatives on a more detailed basis without necessarily making any change to the structure or make up of the SWA Board.

Workplace Gender Equality Agency (WGEA)

10.64 Master Builders supports the policy outcomes pursued by WGEA. However, scope exists to:

- improve the reporting obligation to ensure the associated regulatory burden is minimised as far as practicable; and
- ensure that businesses who comply with reporting obligations are provided with better and more useful information about the results of the data collection process.

10.65 Regrettably, some employers hold the view that there is little useful information or practical information outcomes made available to them once the reporting process has completed. We would encourage the Government to ensure that information, reports, publications or any other like outcomes of WGEA data analysis is published in such a way as to better assist employers both generally and in a more practical sense.

10.66 In addition, the WGEA website (as at 10 January 2017) has a number of links to existing research publications and analysis, however much of this is from non-domestic sources such as Europe or the United States. The quantity of Australian based research is less extensive and on topics which may not necessarily be as relevant as they could be. The Government should consider reviewing the WGEA research processes to evaluate the extent of scope for greater industry and employer input into future activity.

Fair Entitlement Guarantee (FEG)

10.67 Master Builders notes that the Government has decided to not proceed with a previously announced initiative to align payments available under the Fair Entitlements Guarantee to those set by the National Employment Standards (NES). Master Builders seeks that the Government reverse this position and return to its former policy position.

10.68 The existing operation of FEG is problematic in that entitlements set by an enterprise agreement will be covered by FEG notwithstanding that they are significantly larger than those required by the NES. The moral hazards associated with such a practice are trite.

10.69 The Government should be cognisant of the signal such a scheme sends to taxpayers when they become responsible to cover the cost of over-minimum entitlements agreed without Government scrutiny at the workplace level. Such an arrangement also operates to the detriment of small business that are frequently without such arrangements or cannot agree to them due to potential cost. This makes such small business workplaces less attractive to potential employees and distorts the availability of labour.

10.70 Master Builders support recent MYEFO announcements to increase recovery efforts to increase FEG scheme efficiency.

Asbestos Safety and Eradication Agency (ASEA)

10.71 Master Builders is a member of the building, construction and demolition sector committee of ASEA. Master Builders supports the work of the agency and its National Strategic Plan and recognises the importance of the safe removal and remediation of asbestos where appropriate. The Agency should continue to maintain a practical focus with an emphasis on education and providing advice to DIY home renovators, a group that are becoming increasingly at risk of asbestos-related diseases.

Heydon Royal Commission – Related Matters

10.72 Master Builders welcomed the MYEFO announcement of additional resources for agencies involved with, and related to, the Heydon Royal Commission.

10.73 We particularly note the additional resources for the Australian Federal Police, the Australian Competition and Consumer Commission and the Registered Organisations Commission. Given the nature of matters and the complexity of issues dealt with by the Heydon Royal Commission, it is important that law enforcement and other regulatory agencies involved in any matters arising from the Heydon Royal Commission have the necessary expertise, knowledge and experience to appropriately investigate and enforce the law.

10.74 Master Builders would support additional resources being provided to the AFP on a recurrent basis to ensure that the work of its taskforce can continue and that it be established as a permanent entity. To that end, we would seek that at least $2m per year or $8m over the forward estimates be provided to the AFP for a specialist taskforce. To offset such additional expenditure to the AFP, the Government may consider diverting resourcing provided to the FWO. Given the increased duties and responsibilities of the ABCC are now such that it covers 10% of the country's workforce, the FWO resourcing budget may be commensurately reduced and diverted elsewhere within the Portfolio.

Workplace Health and Safety (WHS)

10.75 Master Builders supports the Government's policy of reducing red tape in WHS through working cooperatively with state and territory Governments to develop harmonised WHS legislation. Master Builders' policy position is that quality, rather than quantity, in WHS regulation will assist to improve the performance of the sector and that this will require adequate Government resources being made available especially given the diversity of commencement dates and individual State and Territory differences, even in the context of the harmonised WHS framework.

10.76 Master Builders emphasises the point that greater levels and more strict WHS duties do not of themselves improve WHS performance. To be effective, WHS regulation must also focus on education and awareness, injury prevention and the practical and achievable management of foreseeable risks. Master Builders is committed to improving WHS performance in the building and construction industry, including bringing about cultural change. Harmonisation of WHS has the potential to be an important catalyst for further improvements in performance both in the building and construction industry and more broadly, provided that sufficient emphasis is given to these aspects of WHS regulation, a matter drowned in the current rush of new regulation, especially Codes of Practice.

10.77 The Government should extend efforts to encourage those remaining states who have not adopted the Model legislation to do so. In addition, those states that have adopted model laws should be monitored to ensure that changes made to them at an individual jurisdictional level only occur where absolutely necessary so as to ensure the benefit of a harmonised regime is not undermined.

The Abuse of Safety for Industrial Purposes

10.78 Workplace health and safety requires the active participation of all parties, which is reflected in the model Work Health & Safety laws' emphasis on coordination, cooperation and consultation. At least three Royal Commissions have confirmed the regrettable and long standing practice of construction unions using safety stoppages as a device to advance industrial objectives, as it is relatively easy to mask industrial issues given the ever changing nature of hazards on construction sites. The abuse of safety frustrates cooperation, devalues the importance and the role of safety and by doing so can expose workers at the site to needless risks to their health and safety.

10.79 To combat the abhorrent, tactical use of safety as an industrial weapon the previous *Building and Construction Industry Improvement Act 2005* (BCII Act) placed the burden of proving that a safety stoppage was based on a reasonable concern by the employees about an imminent risk to their health or safety. The *Fair Work (Building Industry) Act 2012* (FWBI Act) reversed this position, placing important advances in safety management and practices in jeopardy.

10.80 While a more appropriate successor to the initial BCII Act sought to restore its initial position, amendments made during its passage saw the status quo preserved. The situation must be restored to that as originally proposed.

The Office of the Federal Safety Commissioner (OFSC)

10.81 The scheme under which the OFSC exists has grown considerably both in terms of the number of companies accredited and the number (and value) of projects within the purview of the scheme. Master Builders previously called for a comprehensive, independent review of the accreditation scheme and welcomed the Governments adoption of this position.

10.82 Master Builders submits that improvements arising from the review about the operation and effectiveness of the Accreditation Scheme will benefit both regulators and the industry. Notwithstanding this, the Government should continue to ensure that the red-tape burden associated with accreditation remains constantly scrutinised and opportunities to reduce said burden are adopted wherever they exist. This is particularly relevant for those building and construction industry participants that are small or medium sized.

Employment Support Programmes

10.83 The extent to which the building and construction industry utilises various programmes employment support programmes is not commensurate with the size of its labour force. Master Builders acknowledges improvements arising from the implementation of the JobActive network however the nature of the sector and the associated workforce skill requirements is such that the majority of its labour force is drawn from other sources. Further, programmes such as the Youth Employment Package and the jobs PaTH Program, while having significant merit, have little application to employers in this sector due mainly to restrictions contained in Modern Awards. Master Builders has brought proceedings before the Fair Work Commission to remove these barriers to youth employment.

10.84 Master Builders would recommend that the Government assess the JobActive network with a view to improving its relationship to other agencies and workplace related program providers such as the Australian Apprenticeship Support Network, vocational education providers, and related programmes. There exists scope for greater coordination between those entities so as to reduce complexity for employers, young people and their parents so as to make a career in the building and construction industry (and/or a trade career generally) more attractive to young people and easier for parents and their advisers to navigate.

Registered Organisations Commission (ROC)

10.85 Master Builders welcomed the passage of legislation to create a Registered Organisations Commission. Given the extensive history of malfeasance amongst building industry unions, the ROC is expected to have a significantly positive impact on the conduct of employee associations in the sector which will be to the benefit of workers and union members.

10.86 Master Builders was one of a handful of organisations that publicly supported the ROC when first announced as policy and remains perplexed as to the positions adopted by other similar groups. Increased transparency and accountability are concepts that ought to be embraced without question.

10.87 While its passage through Parliament was a positive development, Master Builders remains concerned about the effect of, and implications arising from, a number of legislative amendments that changed the law from that as it was initially proposed. Master Builders would support any move by the Government to amend the legislation to reflect its original form.

Secondary Boycotts

10.1 Master Builders supports the Harper Review recommendation (Recommendation 36) on the prohibition of secondary boycotts in sections 45D-45E of the Competition and Consumer Act (2010) to be maintained.

10.2 Master Builders believes that public enforcement of the secondary boycott provisions is inadequate, a point emphasised in the Interim Report of the Royal Commission into Trade Union Governance and Corruption. Timely and effective public enforcement serves as a deterrent to boycott activity and needs to exist both in regulatory culture and capability. Master Builders supports the recommendation for the ACCC to pursue secondary boycott cases with increased vigour, although as an interim measure.

10.3 We submit that following a 12 month period, informed by the increased availability of data about actions taken in this area compared with complaints made, Government will be able to assess whether the required increase in vigour has become manifest. If not, further reform options should be considered

10.4 Master Builders supports the recommendation for the maximum penalty level for secondary boycotts to be the same as that applying to other breaches of the competition law.

Conclusion

10.5 The building and construction industry and the community would benefit from comprehensive workplace relations reform. Legislating the Master Builders' recommendations and adopting other changes to agency resourcing and function would be a vital step on the path to increased productivity.

11 Workforce Skills

Greater investment in vocational education will give young people the skills they'll need for the future

Policy Recommendations:

98. Targeted measures to **assist and encourage employers to take on more apprentices** and to increase the completion rates of building trades apprenticeships, including the return of, and increases to previously available incentive programs
99. **Targeted pre-apprenticeship programs** that support site-ready and productive apprentices to boost business productivity and improve safety in the workplace
100. Significantly boost **financial assistance to building and construction industry employers who invest in the training and mentoring** of young people while completing their apprenticeships.
101. Greater support for industry led programs to **increase female participation in the building and construction industry**
102. **Improved investment in VET** to give young people access to publicly funded industry-focussed training upon completing year 12
103. **Review the national VET training system** to remove current complexities, increase business and parent understanding, and implement consistent funding models
104. **Provide industry with a greater role in determining quality training outcomes from RTOs** by allowing industry to provide feedback on their performance
105. Better support for **mentoring programs** that are proven to increase apprenticeship completions
106. More support for **partnership programs between VET and tertiary education providers**, specifically to develop pathways between construction trades and engineering and construction management higher education degrees

11.1 Master Builders Australia seeks a vocational education and training system that meets the needs of the building and construction industry. The industry is one of the key growth sectors of the economy, which is being constrained by shortages of skilled labour.

11.2 The building and construction industry employs approximately 1.1 million Australians, which represents around 9 per cent of total employment. The industry is the largest employer of skilled tradespeople in the Australian economy with approximately two thirds of the workforce employed in skilled roles.

11.3 Master Builders projects that the building and construction industry will require an additional 300,000 people over the next decade, a 30 per cent increase on the current workforce.

11.4 Master Builders' policy priorities for training are set out in our Towards 2020: Policy for Australian Apprenticeship Reforms and include three main themes:

- Training our workforce
- Quality vocational training structures
- Attracting our future workforce

11.5 Achieving improvements in 'training our workforce' is essential to supporting growth in the Australian economy.

11.6 The current apprenticeship system is in need of a major review to address how more young people can be attracted to work in the trades, how employers can be supported to take young people on, and how the training system can deliver flexible and effective skills for the future.

11.7 Master Builders recommends the Federal Government maintain investment in post-secondary education, particularly skills training, commensurate with future needs of the building and construction industry. At a time when the proportion of skilled jobs is increasing, the number of State-funded training places has been static while Commonwealth investment in skills has been falling.

11.8 Master Builders seeks new investment in building and construction training to support the 60,000 new entrants that will be required each year to meet the projected employment growth of 300,000 people over the next decade and to replace some 30,000 workers who leave the industry through attrition each year. Master Builders recommends an Australian Construction Industry Training Fund be established, which is industry led, to drive quality training outcomes for the industry. Master Builders recommends that an Australian Construction Industry Training Fund be established with a budget of $60 million over three years to support construction industry training. The Fund would provide subsidies to RTOs and industry to support training new entrants and to upskill existing workers, set construction training delivery benchmarks and assess RTOs against these benchmarks to drive an industry-centred quality regime, and work to harmonise construction training and outcomes nationally.

The Fund would improve transparency to consumers on the training being offered and delivered by RTOs through a ratings system.

11.9 Master Builders estimates that completions of construction trades apprenticeships need to more than double over the current decade in order to meet employment demand for skilled tradespeople. Master Builders seeks reforms that can deliver effective assistance to employers and apprentices and harmonise training and apprenticeship regulation within Australia.

11.10 Group Training Organisations (GTOs), which have a significant role in construction apprenticeships owing to the project-based nature of construction work, have been particularly hard hit with decreases in subsidies. Master Builders recommends a review of policies with the aim to support GTOs to undertake their very important role in developing apprentices for the construction industry and a corresponding review of the subsidies available to GTOs to undertake the important work they undertake in employing many young apprentices.

11.11 The basic employer incentive for taking on and retaining adult apprentices has been static at around $4,000 for many years, which represents a only small percentage of the net cost of on-the-job training, administration and wages. Employer incentive payments are even more an imperative against the background of increasing wages and conditions being imposed as a consequence of industrial relations decisions such as competency based wage progression.

11.12 In the short term, limited and tightly targeted financial assistance to employers should be the most appropriate policy response to dealing with a looming skills crisis. Assistance could have the following key elements:

- Re-phasing the standard employer incentive ($1,500 at commencement and $2,500 at completion) to $1,500 at commencement, $1,500 at 18 months and $1,000 at completion, in recognition that apprentices who make it through to third year are more likely to complete their studies. Further, as the payment has been static for many years, a 15% increase over the next three years should be considered to support employers to ultimately lift apprenticeships; and,
- Introduce a 'sign-on' bonus of $3350 on top of the standard employer incentive for construction trades in demand to support employers to employ apprentices

to help meet the need for an additional 300,000 skilled workers over the coming decade.

11.13 Achieving improvements in 'quality vocational training structures' is essential to supporting growth in the Australian economy.

11.14 Master Builders recommends an implementation of a quality VET system with an increased focus on skills attainment outcomes. The Australian Skills Quality Authority (ASQA) should work more closely with industry to identify and respond to instances of poor practice, without increasing the red tape and cost burden on all providers. Auditors should have experience in the construction industry when auditing construction courses. Master Builders seeks an independent ratings system for RTOs that can provide advice to consumers on the quality of delivery for each RTO. The proposed Australian Construction Training Fund could play a significant role in achieving enhanced VET outcomes.

11.15 Master Builders seeks ongoing reforms that will improve the vocational education and training system, particularly in ensuring industry's confidence in the quality of training delivery and in the qualifications being issued, which will elevate trades to the centre of the economy and focus on ensuring Australian workers are highly skilled and job ready.

11.16 Achieving improvements in 'attracting our future workforce' is essential to supporting growth in the Australian economy.

11.17 Master Builders recommends that the Government considers an investment into promoting careers in the building and construction industry in Australian schools. There is wide misunderstanding amongst students, teachers and careers officers of the requirements and attributes that students should possess to be successful in the construction industry. Master Builders recommends that the Government considers a $5 million investment over three years for engaging school students, teachers and career advisers in a careers information initiative that is industry led and implemented. The initiative would directly engage students and teachers in their schools with information on jobs, pathways, employer expectations, VET qualifications, employment opportunities, GTOs and what to expect as an industry apprentice.

11.18 In relation to higher education, Master Builders National Survey has revealed persistent difficulty in filling highly skilled professional positions in the industry across all stages of the economic cycle. This challenge is likely to worsen, as growth in demand for highly skilled roles will far exceed demand for other roles in coming years.

11.19 Master Builders recommends the Federal Government work with industry and education providers to implement a multi-faceted approach to enlarging the pipeline of engineers and construction professionals. Such an approach would promote increased interest in engineering and construction management among school leavers, facilitate closer industry linkages to undergraduate programs, and enhance career development opportunities for early career graduates.

12 Infrastructure

Australia needs more infrastructure to improve our economic productivity and the liveability of our communities in regional areas and cities

Policy Recommendations:

107. Increase private sector investment in infrastructure**, with a target of 6 per cent of GDP for public infrastructure investment across all levels of government.**

108. Expand the use of privitisation models. **Revenue from the sale of existing infrastructure assets should be used to fund the development of new infrastructure.**

109. **Developing and marketing** tradable public infrastructure bonds **on terms of trade and conditions which appeal to a broader spectrum of investors.**

110. **Redirection of government outlays away from recurrent and less productive spending, toward** investment in efficiency and competitiveness enhancing infrastructure**.**

111. Better policy coordination among the levels of government. **The Federal Government should lead a plan, through COAG, to address Australia's growing infrastructure needs.**

112. **Minimising bid costs for infrastructure supply and financing to ensure the broadest possible range of engagement by potential investors.** Tendering processes for smaller investors should be simplified.

113. Reducing the political risk associated with investment in infrastructure. **This would involve focusing on 'stop-start' government decision making, and the tendency for the constant changing of processes, rules and other key elements of a project once underway.**

114. Master Builders supports measures outlined under **Recommendation 9 of the Harper Review**. *"State and territory Governments should subject restrictions on competition in planning and zoning rules to the public interest test, such that the rules should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the rules can only be achieved by restricting competition."*

115. Master Builders supports a recommendation to **review Government procurement policies and policies pertaining to other commercial arrangement with the private sector**, including procurement policies, commissioning, private-public partnerships and privatisation guidelines – **Recommendation 18 of the Harper Review** (2015)

Infrastructure Investment

12.1 Master Builders welcomes the commitment by Government to promote private sector infrastructure investment through its $50 billion infrastructure package.

12.2 However, Master Builders does not support the removal of around $600 million in funding for the Asset Recycling Initiative at a time when Australia is facing an infrastructure shortfall of over $700 billion.

12.3 The Federal Government's reforms to the governance of Infrastructure Australia will create a more independent and transparent body, better able to develop a national view on infrastructure and to derive better value for money in relation to spending on projects of national economic significance.

12.4 A high-quality infrastructure base is vital to Australia's productivity, international competitiveness and sustained economic growth and development. A lack or shortfall in adequate infrastructure is a risk to Australia's future economic growth and productivity.

12.5 Australia faces a major infrastructure challenge over coming decades, both in the maintenance and the remediation of existing infrastructure assets, and investing strategically in expanding our infrastructure base. This is particularly the case in our major capital and regional cities and towns.

12.6 This 'infrastructure challenge' could amount to around $30 billion annually for the decade to 2020, with financial institutions estimating it could cost between $600 billion and $770 billion to deal with existing infrastructure gaps alone.

12.7 The public sector has for many years failed to adequately finance Australia's core infrastructure needs and appears even less likely to be able to do so in the future, pointing toward an even greater role for the private sector in infrastructure supply. Public sector spending on infrastructure, at around 3 to 4 per cent of gross domestic product (GDP), has been inadequate to supply key economic and social infrastructure, and should be lifted progressively to at least 6 per cent of GDP by 2020.

12.8 All levels of Government need to:

- redirect spending from recurrent and less productive expenditures, toward investing in efficiency and competitiveness enhancing infrastructure

- improve policy co-ordination within, and across, the various tiers of Government, with the COAG taking the lead in developing an integrated plan for Australia's economic and social infrastructure needs; and

- remove impediments, such as unfavourable capital-raising, regulatory, taxation regimes, to greater private sector investment in infrastructure.

12.9 Master Builders calls for a broader and deeper role for the private sector in infrastructure supply in Australia. However this should not simply substitute for inadequate public sector infrastructure supply especially in uneconomic (both still fundamentally worthwhile) and/or social infrastructure which is the proper role of the public sector.

12.10 The private sector can contribute to closing Australia's existing and prospective infrastructure deficits by:

- more efficient provision of current infrastructure through, for example, the privatisation of existing infrastructure assets.

- supplying, whether in the form of construction, operation and maintenance, appropriate infrastructure, in particular of an economic nature, beyond that provided by the public sector alone (known as 'additionality').

12.11 Master Builders calls for greater engagement by superannuation institutions in financing infrastructure assets, whether by purchasing existing infrastructure assets (that is, privatisation; with revenues being used for 'capital recycling'); and/or funding the creation of net new infrastructure assets ('additionality'), either directly or indirectly (through the purchase of special purpose tradeable financial instruments).

12.12 While Master Builders shares the wider business concern at the inadequacy of our national infrastructure base, we remain firmly of the view the primary function of Australia's superannuation industry is to provide retirement incomes for superannuation fund holders, with investment strategies and practices of superannuation institutions directed solely toward delivering the optimal risk-return outcomes for fund holders.

12.13 Against this background, Master Builders would oppose mandatory requirements for superannuation institutions to invest (or not invest) in any particular asset classes or products. Rather, Master Builders considers infrastructure to be one of a range of potentially suitable asset classes which a diversified superannuation fund could constructively consider for allocating some part of its investment profile.

12.14 Master Builders calls for a two pronged policy approach for improving the financing of Australia's infrastructure needs, by the:

- public sector – increased direct financing of public economic and social infrastructure, and in identifying and then remedying regulatory and other Government-sourced barriers to the effective operation of the infrastructure supply market;
- developing institutional structures that promote efficient infrastructure investment decisions; and, the
- private sector – identifying and then actioning market-based opportunities, for example in matching the demand-side (infrastructure providers) with the supply-side (financial institutions and other interested investors).

12.15 Key elements of the policy which are properly the function of the Government/ public sector include:

- increasing the direct public sector spending on key economic and social infrastructure (across all levels of Government) to at least 6 per cent of GDP by 2020;
- minimising bid-costs for infrastructure provision/financing to ensure the broadest possible range of engagement by potential investors (including simplified and streamlined processes for smaller investors in infrastructure);

- minimising the political risk associated with investment in infrastructure, in particular ‘start-stop’ decision-making, and changing the processes, rules or other key elements of a project once underway;

- expanding the use of privatisation or other mechanisms for the transfer of existing and prospective infrastructure assets to the private sector, including ‘capital recycling’ (using revenue from the sale of existing infrastructure assets to fund the development of new infrastructure); and,

- developing and marketing, as appropriate, public infrastructure bonds as tradeable financial instruments on terms and conditions which appeal to a broad spectrum of investors.

12.16 Key elements of the policy which are properly the function of the private sector include steps by:

- financial institutions and other investors to broaden and deepen their capacity to evaluate the absolute and the relative merits of infrastructure as an asset class, and specific infrastructure projects as investment vehicles within a diversified investment/lending portfolio.

- financial institutions and other investors to obtain better information on opportunities for investing in infrastructure, either on their own, through relevant industry or professional associations, and in conjunction with counter-parties in the infrastructure supply chain.

12.17 The financial sector more broadly, including the investor community and infrastructure providers, to create tradeable financial instruments, such as private infrastructure bonds, which could be used to finance infrastructure projects in denominations which appeal to a broader range of investors (in particular, smaller investors).

Cities Policy

12.18 Master Builders supports the Federal Government's Smart Cities Policy, to make our cities more liveable, more productive, and more prosperous.

12.19 The essential principle underlying any robust and sustainable 'cities policy' (which must interface seamlessly with 'regional policy') must involve allowing key markets to work better, promoting more market-responsive decision-making, and facilitating equality of opportunity, rather than prescribing rigid interventions and/or given outcomes which favour those who live and work in cities over those who choose to live and work elsewhere.

12.20 As part of the Governments recently announced Smart Cities program, Master Builders supports the Government's initiatives, to invest in smart and more efficient energy technologies to put downward pressure on energy bills, as well as the $100 million per year investment target.

12.21 Master Builders also supports the establishment of the Commonwealth governments $50 million competitive Smart Cities Program, to support local governments to collaborate and apply innovative technology-based approaches to improve the liveability of cities and their suburbs, and provide incentives to open up their data and partner with other regional stakeholders.

12.22 Master Builders also supports the proposal for a record investment of $50 billion between 2013-14 and 2019-20 on road and rail projects across Australia: reducing congestion, improving the liveability of cities and connecting our regions to markets.

Planning and Zoning

12.23 Anti-competitive land and zoning policy must be addressed as a first priority if housing affordability, and the challenges of first home buyers seeking to enter the housing market are to be addressed seriously. Restrictive land policies by state/territory and local Governments are not in the public interest and would likely fail any public interest tests (as outlined under Recommendation 8 of the Harper Review (2015)).

12.24 Further to Recommendation 8, Master Builders supports measures outlined under Recommendation 9 of the Harper Review (2015). "State and territory Governments should subject restrictions on competition in planning and zoning rules to the public interest test, such that the rules should not restrict competition unless it can be demonstrated that the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the rules can only be achieved by restricting competition."

12.25 The following competition policy considerations should be taken into account:

- *Arrangements that explicitly or implicitly favour particular operators are anti-competitive.*
- *Competition between individual businesses is not in itself a relevant planning consideration.*
- *Restrictions on the number of a particular type of retail store contained in any local area is not a relevant planning consideration.*
- *The impact on the viability of existing businesses is not a relevant planning consideration.*
- *Proximity restrictions on particular types of retail stores are not a relevant planning consideration.*
- *Business zones should be as broad as possible.*
- *Development permit processes should be simplified.*
- *Planning systems should be consistent and transparent to avoid creating incentives for gaming appeals.*

12.26 Planning regulations should work in the long-term interests of consumers. They should not restrict competition unless the benefits of the restriction to the community as a whole outweigh the costs, and the objectives of the regulations can only be achieved by restricting competition.

12.27 One area that should be subject to an immediate competitive review is the land release policies of state/territory and local Governments. Land is an important input to the production of goods and services and a source of amenity for consumers. Even small policy improvements in this area could yield large benefits to the economy.

12.28 Master Builders supports the formation of an independent body such as the Australian Council for Competition Policy (APCC) as outlined under Recommendation 43 of the Harper Review (2015), and is responsible primarily for reporting on the progress of State and Territory Governments in assessing planning and zoning rules against the public interest test. Master Builders supports recommendations, including:

- *A mandate to provide leadership and drive implementation of the evolving competition policy agenda.*
- *The ACCP should be established under legislation by one State and then by application in all other States and Territories and at the Commonwealth level. It should be funded jointly by the Australian Government and the States and Territories.*
- *The ACCP should have a five member board, consisting of two members nominated by state and territory Treasurers and two members selected by the Australian Government Treasurer, plus a Chair. Nomination of the Chair should rotate between the Australian Government and the States and Territories combined. The Chair should be appointed on a full time basis and other members on a part time basis.*

Government Procurement

12.29 Master Builders supports a recommendation to review Government procurement policies and policies pertaining to other commercial arrangement with the private sector, including procurement policies, commissioning, private-public partnerships and privatisation guidelines. Procurement and privatisation policies and practices should not restrict competition unless:

- the benefits of the restrictions to the community as a whole outweigh the costs; and
- the objectives of the policy can only be achieved by restricting competition.

12.30 An independent body, such as the Australian Council for Competition Policy, should be tasked with reporting on progress in reviewing Government commercial policies and ensuring privatisation and other commercial processes incorporate competition principles.

12.31 The substance of Recommendation 18 of the Harper Review (2015) is endorsed.

13 Immigration

Policy Recommendations:

116. Setting the **permanent migration intake at between 200,000 and 240,000 per year**, with a focus on skilled migration

117. **Review the 'highly skilled' threshold within employer-nominated visa classes** to reduce ongoing skills shortage in 'middle and semi-skilled' occupations and resulting project bottlenecks

118. The '457 visa' program should remain uncapped and responsive to the nation's skills needs with the migration program filled by people who have previously held a temporary visa in Australia. **Labour market testing should also be removed.**

13.1 Master Builder's overarching policy principle is to support a strong migration program, particularly for economic and skilled migration. However, in doing so we are strongly committed, first and foremost, to the training and upskilling of Australians and to supporting local employment.

13.2 A well-managed and -targeted immigration program is an important policy lever which brings a range of social and economic benefits to Australia. It adds to the supply of skilled labour, increases accumulated savings and contributes to domestic investment and expanded domestic consumption. Immigration also brings indirect benefits by increasing innovation and connectedness with the rest of the world, and by promoting a vibrant, cosmopolitan and outward-looking Australian culture that is better equipped to meet the challenges of the future.

13.3 The cyclical nature and periods of high levels of investment and activity in the building and construction industry means employers often need to supplement the local labour force with skilled migrants.

13.4 In this context, the building and construction industry continues to face serious labour force challenges, relating both to an expected increased demand for managerial, skilled and unskilled labour and to replacing the exiting and/or retirement of a sizeable number of skilled workers over the next decade.

13.5 Master Builders estimates, based on current industry labour force attrition rates and growth projections, around 60,000 entrants to the industry will be required each year, on average, over the next decade with around two-thirds (or some 40,000 people) of this demand being for skilled positions. These figures compare with construction trades apprenticeship commencements of 23,900 in 2015, where generally some 65% will not complete their full qualification.

13.6 Managing the immigration program to achieve an optimal flow of migrants will help maximise the economic and social benefits they offer and contribute to ensuring Australia's longer-term social and economic needs are met.

13.7 Master Builders recommends the Federal Government pursue an annum Net Overseas Migration (NOM) program intake of between 200,000 and 240,000 persons. This figure reflects our commitment to a 'bigger Australia' and increasing skills pressures across a number of sectors of the Australian economy, and in the building and construction industry in particular.

13.8 At the same time, a targeted skilled migration program is needed to ensure Australia's economic and productivity potential is realised. Against this background, at least two thirds of Australia's permanent migrants enter through the Skill stream.

13.9 In addition to helping to address skills shortages, the program intake must take into account the changing skill needs of the labour market.

13.10 Due to the project nature of work in the construction industry, the migration program intake needs to help business and industry meet labour requirements during peak periods of employment, where skill shortages can become a significant barrier to successfully completing construction projects.

13.11 Against this background, the '457 visa' program should remain uncapped and responsive to the nation's skills needs with the migration program filled by people who have previously held a temporary visa in Australia.

13.12 Master Builders believes labour market testing for 457 visas is unnecessary and should be removed. This position is echoed by the OECD, which has previously pointed out that employer-conducted labour market testing is not "fully reliable", and in the Australian context has proven ineffective.

13.13 The Federal Government should also enhance access of certain occupations, currently classified as 'semi-skilled' for the purposes of permanent employer-sponsored migration which could best be achieved by including priority semi-skilled on the Employer Nominated Skilled Occupation List on a case-by-case basis; and apply a functional English standard for skilled migrants, consistent with the ability to read and understand workplace instructions and safety standards.

MASTER BUILDERS
AUSTRALIA

UNLOCKING SUPPLY

Keeping home ownership within reach of all Australians

May 2017

CONTENTS

Denita Wawn
Chief Executive Officer
Master Builders Australia

FOREWORD

Homeownership is a part of the Australian way but it's becoming harder for many Australians to attain.

Master Builders believe the most effective and sustainable solution to keeping homeownership within reach is building more new homes to meet demand but the industry has been faced with increasing land costs and delays that create roadblocks to increasing supply.

Master Builders has continuously advocated for policies to pare back the costs, red tape and regulatory creep that are impediments to increasing supply and which drive up house prices — it's estimated by as much as 30 to 40 per cent.

We believe that the Federal Government can play a role by providing financial incentives to state and local governments and increasing infrastructure spending — both to be used as levers to remove structural and cost barriers to building more new homes. This approach has been the centrepiece of our housing affordability policy.

In the 2017-18 Federal Budget, the Treasurer announced a Housing Affordability package that reflects our push for resolving the supply bottlenecks.

Economic modelling, commissioned by Master Builders, and carried out by Cadence Economics, shows that these measures will substantially increase the housing supply, create new jobs, boost construction activity and deliver substantial economy wide benefits.

This is great news. We now seek effective implementation of these announcements so we can get on the job and build more houses to keep the Australian dream of homeownership alive.

EXECUTIVE SUMMARY

We know that a shortage of 'shovel ready' land, combined with embedded regulatory and tax costs can amount to 30-40 per cent of the cost of a new home — putting a floor under house prices. Therefore, in order to boost supply which helps housing affordability policy reforms must address both the cost and availability of land for residential development.

The Government's housing affordability strategy, announced in the 2017 Budget, endeavours to directly address the factors which are preventing a more efficient supply of housing and which push up house prices.

At its centre is a $75 billion transport infrastructure package, complimented by an additional $1 billion for investment into infrastructure bottlenecks in residential developments areas.

Master Builders commissioned Cadence Economics to examine what this new infrastructure funding means for housing supply, affordability and the economy between now and 2020-21.

Together, investment funding in the Budget forward estimates is forecast to support the construction of up to 93,000 additional new homes by 2021, boosting supply by 41%.

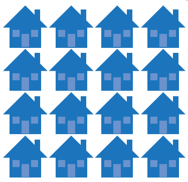
Housing supply is expected to receive an additional boost from the Government's City Deals programme, with local councils in Western Sydney first up to receive financial incentive payments to support housing sector reforms.

Federal infrastructure funding is forecast to support an additional $5.6 billion in activity in the building and construction industry and create up to an additional 4,200 permanent building and construction jobs on average each year.

Households are expected to be $3.2 billion better off, equal to $330 for each and every household in Australia over the next four years. The latter translates into a boost to GDP of close to $2 billion over the period to 2021.

UNLOCKING HOUSING SUPPLY

Budget 2017: Master Builders analysis of Budget infrastructure investment...



93,000 extra homes by 2021

Impact on housing affordability by 2021

- The $75 billion transport infrastructure package to support the construction of up to 75,000 extra homes
- The $1 billion National Housing Infrastructure Facility to support the construction of an extra 18,500 new homes
- Housing supply to be as much as 41% higher as a direct result of new government funding into better housing and transport infrastructure
- Release of surplus Commonwealth land for residential development
- Relieving supply side pressure on house prices

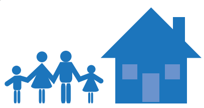
Supporting...

4,200 extra construction jobs

- $75 billion transport infrastructure package to create 3,800 extra fulltime jobs each year
- $1 billion National Housing Infrastructure Facility to create an extra 400 extra fulltime jobs each year

$4.5 billion in extra construction

- $75 billion transport infrastructure package to boost building and construction activity by $4 billion in the next four years
- $1 billion National Housing Infrastructure Facility to boost building and construction activity by $500 million in the next four years



$3.1 billion extra for households hip pocket

- Reducing living costs pressures by an equivalent of $330 per household
- $1 billion National Housing Infrastructure Facility to make households $400 million better off
- $75 billion transport infrastructure package to make households $2.7 billion better off

Adding $2 billion to GDP over the next four years

BACKGROUND

Federal Government investment in infrastructure

"Nothing increases the supply of well-located land like good transport links." (Phillip Lowe, RBA Governor, 2017)

The 2017-18 Federal Budget delivers a significant investment in infrastructure.

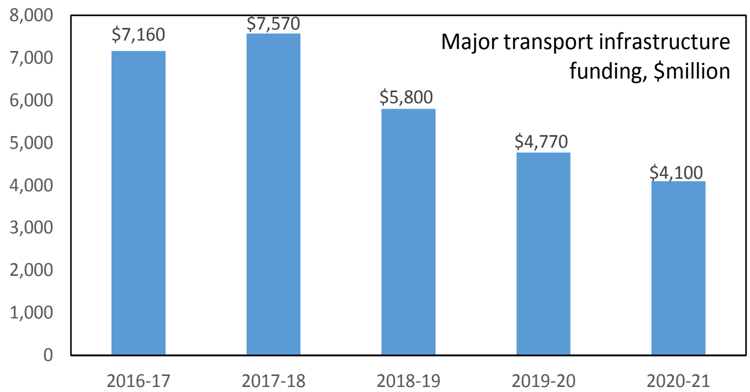
At the centre of the Government's infrastructure investment strategy is a commitment of $75 billion in funding and financing from 2017-18 to 2026-27 for critical road, rail and airport infrastructure, led by a $20 billion commitment to upgrade Australia's passenger and freight rail.

An extra $1 billion has also been put aside to establish the National Housing Infrastructure Facility to address infrastructure chokepoints that are impeding housing development in critical areas of undersupply.

To address rising input costs which reduce land affordability, the Government under the City Deals programme, will offer incentive payments to State and Local Governments to support planning and zoning reform, while an additional $300 million will be offered under a newly established National Partnership on Regulatory Reform which has been set up to fund "reforms that drive Australia's eco performance and living standards".

Suitable surplus Commonwealth land, starting with 127 hectares of Defence land in Maribyrnong, should support up to 6,000 new residential dwellings, and could further boost supply.

Chart 1: Major Transport Infrastructure Funding, Budget 2017-18



Source: Federal Budget, Budget Paper No. 3, 2017-18, Master Builders Australia.

Note: includes funding for all major infrastructure projects listed in Budget Paper No. 3 2017.

Building more new homes

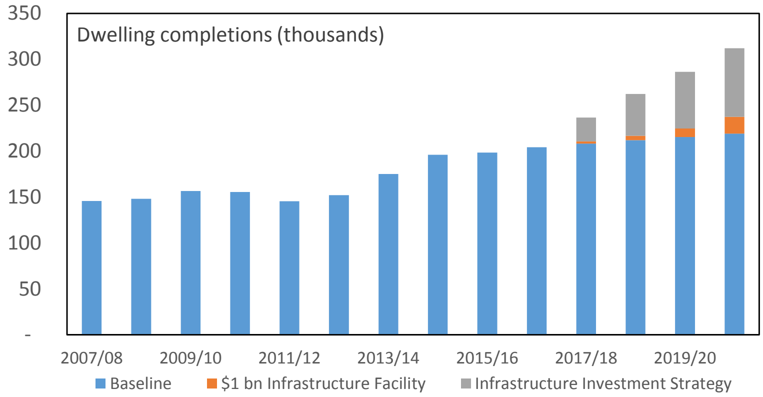
We know that a shortage of 'shovel ready' land, combined with embedded regulatory and tax costs can amount to 30-40 per cent of the cost of a new home — putting a floor under house prices. Therefore, in order to boost supply which helps housing affordability, policy reforms must address both the cost and availability of land for residential development.

"Dwelling construction fell short by 165,000 over the last decade, causing house prices to be higher than they need to be." (Master Builders Australia, 2017)

At its centre is a $75 billion transport infrastructure package, complimented by an additional $1 billion for investment into infrastructure bottlenecks in residential developments areas.

Master Builders commissioned Cadence Economics to examine what this new infrastructure funding means for housing supply, affordability and the economy between now and 2020-21.

Chart 2: Impact on housing supply



Source: Federal Budget, Budget Paper No. 3, 2017-18, Master Builders Australia.

Note: includes funding for all major infrastructure projects listed in Budget Paper No. 3 2017.

Broken down by the two programmes, the $1 billion National Housing Infrastructure Facility is expected to support the construction of an additional 18,500 homes by 2021 (shown above in orange) as a result of targeted investment into areas where infrastructure bottlenecks are limiting future development opportunities.

The expected contribution of the Government's $75 billion infrastructure package for this period is $30 billion and shown above in grey. It is expected to support the construction of up to 74,000 extra new homes by 2021.

Not captured in the chart above is the Government's plan to release suitable surplus Commonwealth land, or the financial incentives for State and Territory Governments to meet housing supply targets.

Under the City Deals programme, the Government will offer incentive payments to State and Local Governments to support planning and zoning reform.

The supply of affordable rental housing will receive direct support through the National Housing Finance and Investment Corporation to operate an affordable housing bond aggregator to provide cheaper and longer-term finance for the community housing sector.

Other measures, including changes to foreign investment rules, which now provide tax incentive for foreign investors into social housing, and changes which allow Managed Investment Trusts to acquire, construct and redevelop social housing, will also support a greater share of private foreign investment into the social housing sector.

Master Builders believes that the supply measures in the Government's Housing Affordability Package should help to unlock supply and reduce land costs on city fringes, improve connectivity in the regions through better transport infrastructure and support a greater level of private investment into community housing to help reduce the waiting list for social housing of 190,000 and growing.

Macroeconomic contribution — economy wide benefits

Infrastructure investment benefits the whole economy through promoting productivity and increasing efficiency and connectivity in our cities and regions.

Federal infrastructure funding in the Budget forward estimates is forecast to support an additional $4.5 billion in activity in the building and construction industry and create on average, an additional 4,200 permanent building and construction jobs each year.

Households are expected to be around $3.2 billion better off, equal to $330 for each and every household in Australia over the next four years. The latter translates into a boost to GDP of close to $2 billion over the period to 2021.

Table 1: Budget Infrastructure Funding Macroeconomic Contribution, 2017-18 to 2020-21

$ millions	2017/18	2018/19	2019/20	2020/21	Total
Construction	790	1,090	1,240	1,340	4,450
Construction Jobs*	3,020	4,140	4,670	4,970	4,200
GDP	210	380	550	780	1,920
Households	480	720	900	1,080	3,180

Source: Federal Budget, Budget Paper No. 3, 2017-18, Master Builders Australia.

Note: includes funding for all major infrastructure projects listed in Budget Paper No. 3 2017. *Construction jobs total presented as an average number of jobs created per year between 2017-18 and 2020-21.

$1 billion National Housing Infrastructure Facility

The Government's National Housing Infrastructure Facility will take $1 billion out of the cost of providing urban infrastructure.

Modelling by Cadence Economics, commissioned by Master Builders, shows this $1 billion investment would unlock a significant amount of new residential land and support the construction of an additional 18,500 new homes — creating an additional 650 permanent building and construction jobs in the economy, each and every year to 2020-21.

With every $1 the Government spends under the National Housing Infrastructure Facility, the household hip pocket should be better off by $1.40.

Or, put another way, the programme is slated to support an additional $1.2 billion in GDP over the next four years, including $1.1 billion in additional building and construction revenue.

But to be successful in achieving its objectives, the funding must be targeted but accessible to ensure local councils are able to take up the opportunity to supplement funding of local urban infrastructure.

$75 billion transport infrastructure package

Correctly targeted 'city shaping' transport infrastructure can effectively boost the supply of housing land ... Such expansion in effective land supply for housing can place downward pressure on house prices." (National Housing Supply Council, 2013)

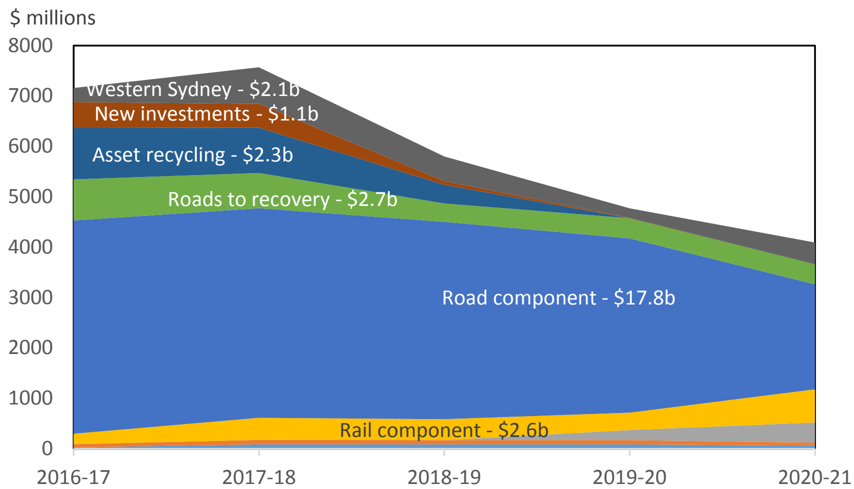
The 2017-18 Budget commits $75 billion in infrastructure funding from 2017-18 to 2026-27.

Of this, the Budget papers include more than $30 billion in funding, this year and over the next four years for critical road, rail and airport infrastructure, forming a centre piece of the Government's economic growth strategy and an important part of its housing affordability strategy.

Major transport infrastructure project funding in the Budget forward estimates is forecast to support the construction of an additional 75,000 new homes by 2021, increasing revenue into the building and construction industry by over $4 billion, and supporting an additional 4,000 permanent building and construction jobs in the economy each year for the next four years.

Households should pocket an extra $2.7 billion over the next four years as a result of better access to housing and more efficient transport links. GDP is expected to be $1.5 billion better off as a result of direct economic contributions from greater transport infrastructure investment.

Chart 3: Budget Major Infrastructure Project Spending



Source: Federal Budget, Budget Paper No. 3, 2017-18, Master Builders Australia.

Note: includes funding for all major infrastructure projects listed in Budget Paper No. 3 2017.

APPENDIX

Modelling Details

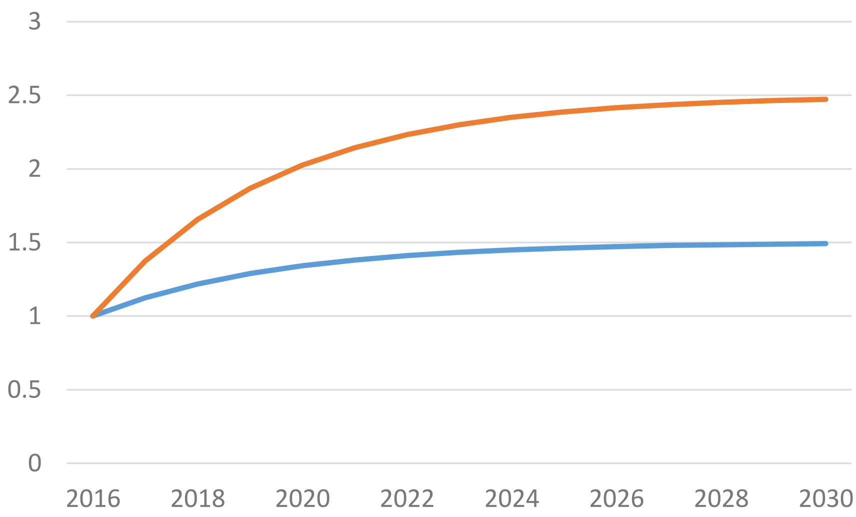
The analysis undertaken in this report relies on a combination of two separate models. The first is the Alonso-Muth-Mills model adapted from the Reserve Bank of Australia's research discussion paper "*Urban Structure and Housing Prices: Some Evidence from Australian Cities*" (Kulish, Richards and Gillitzer, RDP 2011-03). The functional structure of the model is unchanged from that used by Kulish, Richards and Gillitzer, with a detailed description of the model provided in Appendix A of that paper.

The second model used is the CEGEM model, Cadence Economics' in-house Computable General Equilibrium (CGE) model. CGE models are widely used and accepted, having been applied by Australian governments at the state and federal levels for policy issues including the impacts of trade liberalisation, carbon pricing and for taxation efficiency analysis.

The CEGEM model is used to estimate the indirect and economy wide impacts of the specific housing market impacts revealed by the Alonso-Muth-Mills model.

Set against the reference case scenario is a 'scenario projection'. This scenario represents the impacts of imposing a policy shock. The impacts of the policy change are reflected in the differences in the variable at time T. It is important to note that the differences between the reference case and policy intervention scenario are tracked over the entire timeframe of the simulation.

Dynamic simulation using CEGEM



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CONSIDERATION OF MEASURES AIMED AT IMPROVING HOUSING SUPPLY

REPORT FOR MASTER BUILDERS AUSTRALIA

July 2017

1 Executive Summary

Housing affordability is one of the most visible public policy challenges in Australia today. It is a complex policy challenge, with multiple housing markets across Australia operating at different stages in the cycle, facing unique challenges when it comes to housing affordability and home ownership.

The extent of the issue in Sydney and Melbourne is well known, with house prices in Sydney and Melbourne doubling in the last decade. However, the housing markets in Perth and in Darwin face a very different set of challenges, with house prices falling for the best part of two years.

Given this patchwork of conditions it is important that the policy response from Government, particularly at a national level, does not (for example) adversely impact homeowners in Perth and Darwin as a result of policy aimed at curbing house price growth in Sydney and Melbourne.

The Federal Government has rightly acknowledged the need increase the ***supply*** of new homes as the first step in solving the problem of housing affordability in Australia. To do so, the 2017 Federal Budget included a series of measures aimed at increasing the supply of new housing with the ultimate aim of making housing more affordable.

1.1 Why is increasing supply the solution?

At a national level, the past decade has seen a significant shift in the trends for the supply of housing and population growth. Prior to 2004, growth in the supply of housing has historically been higher than population. However since then there has been a moderation and at times a reversal of this longer run pattern whereby population growth has outpaced housing supply.

Housing investment has historically averaged around 6% of GDP. In 2004-05 housing investment fell to around 5.5% of GDP and stayed there for the best part of the following decade. That may not seem like much, but over a decade that 0.5% difference added up to a shortfall in housing investment of close to $83 billion, enough to build an extra 165,000 new homes.

The industry has been playing catch-up in the last two years, with new housing completions outpacing underlying demand since around 2014. But despite a recent period of higher housing investment, the Federal Government estimates Australia's housing shortage still exceeds 100,000 dwellings.

Several reports into the housing sector by the Productivity Commission, the Reserve Bank, the Treasury, and as a recommendation in the Henry Tax review, all find that the housing supply shortage must be solved as a first step in any reasonable strategy to fix housing affordability in Australia.

An alternate view posed leading up to the 2017 Federal Budget was to use the tax system to curb investor activity. The objective being to help affordability by recalibrating the tax settings to give first home buyers and home owners more room in the market.

For the Federal government to address housing affordability through demand side measures is problematic. In the first instance, this is because it is difficult to assess the exact contribution that Federal tax settings have on house prices. But perhaps more important, Federal tax settings are not adjustable by jurisdiction. As such, tinkering with them to curb investor activity in Sydney and Melbourne risks further exacerbating the cyclical downturn in the housing markets in Perth and Darwin.

Changes to the tax system also do not address the main structural issues in the market which put upward pressure on house prices - that is a housing stock which is not sufficient to meet the growing demands of population growth and changing community demographics.

1.2 What can the Federal Government do?

The stock of housing in a particular location is the responsibility of the respective State/Territory Governments. Hence, many of the direct cost imposts such as such as stamp duties, developer charges and land rates are levied at a State/Territory or local government level. Regulation on property and the development of land for different uses is also the responsibility of the States/Territories.

However, there is still an important role the Federal Government can play in supporting reforms, with a number of programs announced as part of the 2017 Federal Budget slated to do just that. The Federal Government has successfully used an incentive model to support reforms at a State/Territory level in the past, perhaps most notably following recommendations of the Hilmer review (1993) into national competition policy.

In this report, incentive payments which support targeted reforms to boost the supply of new housing are examined under three scenarios; (1) measures to reduce the direct costs of residential land development (either through reduced developer charges or more streamlined planning processes); (2) reducing transportation costs through better infrastructure investment; and (3) reducing restrictions on planning and zoning in inner city markets, focussing on building height restrictions.

These three scenarios were selected following a rigorous consultation process with Master Builders membership of residential builders, construction workers and building suppliers, across every State/Territory in Australia, and hence represents the priority issues for reforms which currently limit the supply of more new housing. The issues covered therefore provide a basis for recommendations to be made around the allocation of Federal Government incentive payments across the different housing markets, to provide the most effective and tailored policy response to the challenges of housing affordability.

Developer Charges and Planning Delays

A significant contributor to the cost of new housing developments comes in the form of charges levied on new land developments for utility, transport, communication and other supporting infrastructure. In addition, embedded land costs, including land shortages caused by inadequate land release policies, planning delays as well as other inputs costs all contribute to increasing the costs of development of new residential land.

Two key issues raised during consultation in relation to having adverse effects on housing affordability were developer charges and planning delays.

The exact impost of developer charges is difficult to determine with large variance in the mix of charges levied across states and councils. In Sydney it is estimated that government infrastructure charges alone contribute 12% to the cost of a greenfield new housing development and 5% to an infill two bedroom apartment, while the average across Sydney, Melbourne, Brisbane and Perth is 7% and 4% respectively. Similarly, hard data on planning delays is difficult to obtain.

In assessing the impacts of reduced developer charges or planning delays, the paper makes the conservative assumption that either $500 million in developer charges can be removed from the system (reducing house prices by around 0.5 per cent, a fraction of the total impost from developer charges) or, equivalently, that planning processes can be reduced by one month for new housing developments.

The economic benefits of reductions in developer charges and delays are compelling. Based on these assumptions, and considered individually, each of these reforms A has the potential to add $850 million to Australia's gross domestic product (GDP), in net present value (NPV) terms over the next four years. Household consumption is projected to increase by $1.4 billion in NPV, bringing forward the construction of approximately 36,000 dwellings over this period.

The case for reductions in unnecessary planning delays, or regulatory impost, is particularly compelling, as it comes with no first-round reduction in public sector revenues, and indeed would likely increase government revenues in line with increased activity.

Relaxing Planning and Zoning Restrictions

Policies to limit housing density (such as building height or plot ratio restrictions) reduce the supply of housing to people in those areas, placing upwards pressure on housing prices in inner city regions and shifting the population further towards the urban fringe.

This shift outwards has two impacts – in the first instance, it increases the level of urban density in the mid and outer city regions. In the second instance, the inner city supply restriction and the shift outwards of the population increases house prices across the entire city, both due to the supply constraint in the inner city and due to the demand increase in the mid to outer city region.

To illustrate this differentiated impact by city size we consider comparable zoning restrictions between large, medium and small cities. In a large city this decreases housing prices per square metre by 2.31%. By comparison, in a medium city this same shock leads to a 1.47% decrease, while in a small city the impact is 0.53%.

Finally, planning restrictions such as height or density restrictions are not generally uniformly binding across a city, with the impost likely to be experienced in high growth pockets.

Our estimate of a phased in relaxation of planning restrictions finds that the potential impacts are significant, with a net present value of household consumption of over $500 million and an additional 20,000 dwellings built.

Improvements in Transportation Infrastructure

Announced in the 2017-18 Federal budget was a range of measures intended to improve housing and transport related infrastructure, including the $1 billion National Housing Infrastructure Facility, and $75 billion from 2017-18 to 2026-27 for critical road, rail and airport infrastructure.

The impacts of these budget measures make a $1.15 billion contribution to aggregate household consumption, and add approximately 38,000 houses to the national housing stock. Of the States, New South Wales (with the largest housing market) is set to receive the biggest benefit, with better transport links into the outer suburbs of major cities slated to support the construction of an additional 12,000 homes. Victoria follows closely behind with an additional 10,000 new homes to be built as a result of improvements in its urban transport infrastructure.

Using the detail provided in the cost benefit analyses undertaken for the M4, WestConnex and Melbourne Metro we estimate that private transport benefits account for 24% of the total transport benefits of a representative transport infrastructure project, with an investment of approximately $254 million required to reduce the average travel cost per km by 1%.

2 Introduction

Housing affordability has become one of Australia's most pressing, visible, and widely debated public policy issues. Key to the difficulty of addressing housing affordability is the inherent complexity of the issue, cutting across governments at all levels and with unique constraints and circumstances between cities and states.

Consistent with recommendations from the Productivity Commission, the Federal Treasury, and the Reserve Bank of Australia, this report focus' on key supply side reforms. The subsequent scenario chapters quantify the potential impacts of these supply side reforms, with the aim of providing evidence which may support the allocation of funding under programs announced in the 2017 Budget, such as the new $1 billion housing infrastructure facility and the $375 million affordable housing and homelessness agreement, as well as potential reforms in scope for proposed incentive payments from the Commonwealth Government through the recently commenced City Deals process.

Given that housing markets are predominantly the jurisdiction of state/territory governments, supply side responses from the Federal Government revolve around the ability of incentives (or removal of disincentives) available to increase the size of the housing stock and to lower price pressures on new housing, particularly in greenfield developments.

Effective supply side reform presents the greatest opportunity to increase aggregate welfare to Australian households, achieving the greatest good for the greatest number of people, rather than simply acting as a redistribution mechanism.

This report follows the 2017 Federal Budget, which included a series of measures aimed at addressing the shortage of housing supply and the associated pressure put on housing affordability.

The subsequent scenario chapters in this report provide a breakdown of the potential benefits of reforms into three priority areas:

- Better transport infrastructure, reducing the cost of living further from work;
- relaxation of planning restrictions, allowing for greater density in the inner city; and
- removing constraints on land release and reforming developer charges.

Acknowledging the unique circumstances facing housing markets across the country the analysis in this report is informed both through official and publicly available housing statistics and through direct consultation with Master Builders members.

In doing so, the scenario analysis provides a basis for a targeted approach to regulatory reform in the housing sector, which adequately accounts for the different priority challenges across housing markets in different jurisdictions.

Individually, each of these supply side reforms can guide the structure of Australian cities in significant ways, with subsequent improvements in the welfare of the people who live in them. Improvements in transport infrastructure relax the pressures that result from competition to live as close as possible to work, while appropriate planning, zoning and land release policies reduce the costs and increase the availability of houses in the locations that people choose to live. In this sense, these recommendations are not just about increasing supply. Rather they are about increasing supply of the right type of housing in areas where people want to live – increasing supply and maximising consumer welfare at the same time.

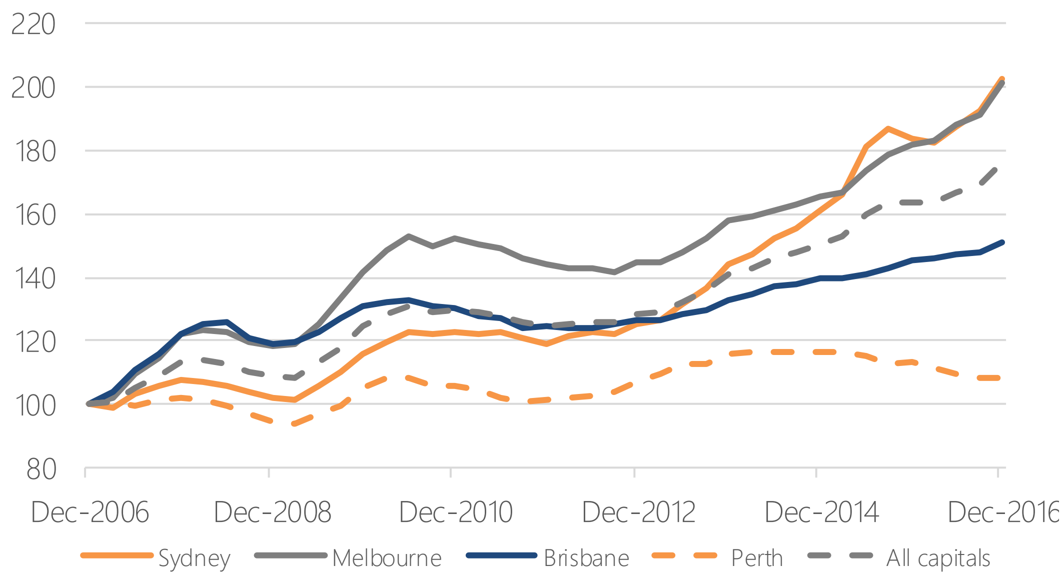
As such, it is hoped that the scenario analysis in this report is used in support of submissions for funding aimed at reforming the key issues identified as holding back the supply of new, more affordable housing in each state and territory.

This report provides a brief analysis of housing affordability and relevant background to the supply side reforms in Section 2. In Section 3 we outline the results of industry consultation, while in Section 3 we apply two specialised modelling frameworks to quantify the housing market and economic impacts of the three supply side scenarios described above. Finally, in Appendix A we provide a brief summary of the industry consultation and in Appendices B and C we provide additional detail of the modelling frameworks applied to address these important questions.

3 Housing affordability and the policy landscape

Housing affordability is one of the most visible public policy challenges in Australia today. The extent of the issue in Sydney and Melbourne is immediately apparent from the Australian Bureau of Statistics housing price index (as shown in Figure 1), while on the other hand, Perth is being challenged by deteriorating house prices.

Figure 1: Comparison of house price indexes



Note: All prices indexed to 100 in December 2006.
Source: ABS 6416.0, Table 7, Residential Property Price Index

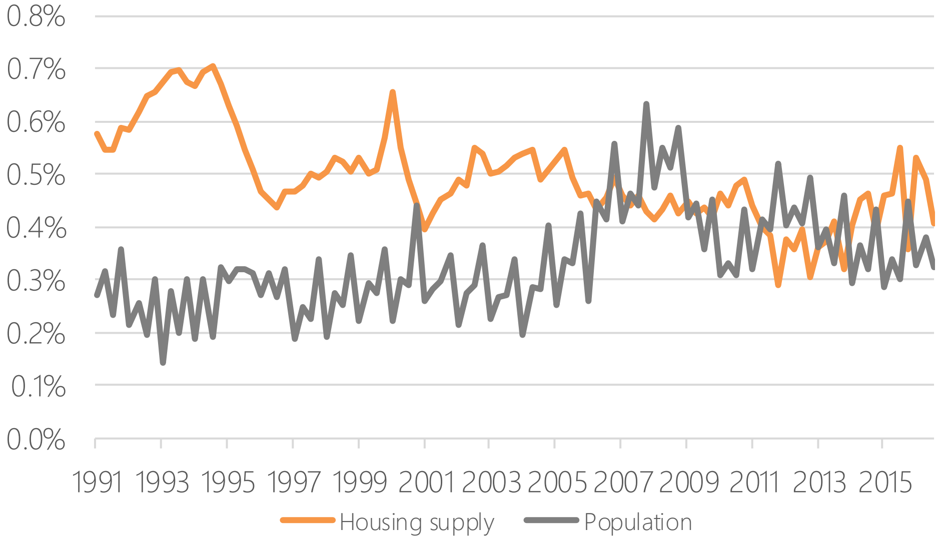
Over half of all Australians live in the four largest population centres of Sydney, Melbourne, Brisbane and Perth, while inclusion of the three remaining capital cities captures 60% of the population.

Much of the focus on housing affordability is on Sydney and Melbourne. However, it is important to note that a range of housing challenges, which often run counter cyclical to the housing challenges in our major population centres, exist in other capital cities and indeed in much smaller cities and regional areas. Effective policy must consider its impact across the spectrum of housing markets in Australia.

3.1 Population Impacts

At a national level, the past decade has seen a significant shift in the trends for the supply of housing and population growth. As shown in Figure 2, growth in the supply of housing has historically been higher, while growth in population has been lower. But more recently, since around 2004, we have seen a moderation and at times a reversal of this longer run pattern.

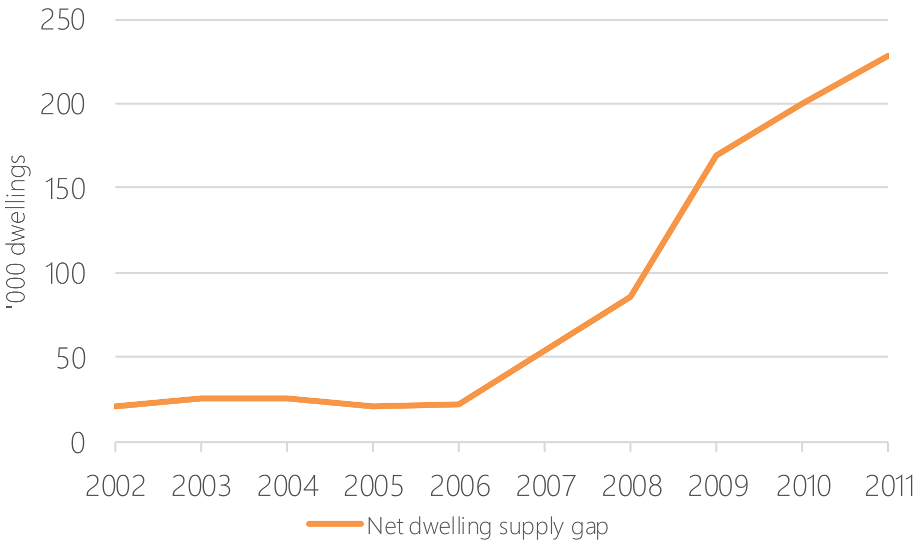
Figure 2: Housing supply versus population growth



Source: ABS 8752.0, ABS 6416.0

While estimates of the degree of housing shortages vary, the consequences of this historical shift were apparent in the National Housing Supply Council report *Housing Supply and Affordability – Key Indicators, 2012*, which found a sharp upturn in the net national dwelling supply gap starting in the mid 2000's, as shown in Figure 3.

Figure 3: Estimated net dwelling supply gap



Source: National Housing Supply Commission, Housing Supply and Affordability – Key Indicators, 2012, Table 4.1

Since 1970, housing investment has averaged 6% of GDP. But in 2004-05 housing investment fell to around 5.5% of GDP and stayed there for the best part of the following decade. That may not seem like much, but over a decade that 0.5% difference added up to a shortfall in housing investment of close to $83 billion, enough to build an extra 165,000 new homes.

The industry has been playing catch-up in the last two years, with new housing completions outpacing underlying demand since 2014. But despite a recent period of higher housing investment, the Federal Government estimates Australia's housing shortage still exceeds 100,000 dwellings. This gap must be filled before supply constraints stop putting upward pressure on house prices.

3.2 Public policy and progress to date

The Productivity Commission[1], while recognising the role that the taxation system has played in increasing the demand for housing, provided the following comment on the proposed changes to property taxation:

> *Attempting to address these impacts for housing alone would be hazardous. Indeed, ostensibly 'quick fixes' suggested by many participants — such as limiting negative gearing or removing the CGT discount for housing — could detract from rather than promote more efficient investment. Hence, the Commission considers that a broader examination is needed.*

The PC went on to make the following recommendation:

> *The Australian Government should, as soon as practicable, establish a review of those aspects of the personal income tax regime that may have recently contributed to excessive investment in rental housing. The focus of the review should be on the Capital Gains Tax provisions. However, it should also assess 'second best' options for addressing distortions in incentives to invest in housing and other asset markets, including: restrictions on negative gearing and changes to the capital works deduction provisions for buildings. Pending such review, it would not be appropriate to make housing-specific changes to negative gearing rules or to capital gains tax arrangements.*

It then went on to say [emphasis added]:

> *As noted, there are inherent constraints on the capacity of housing supply to respond to surges in demand in a way that could* ***greatly moderate price rises****. That said, in many parts of Australia, it appears that regulatory processes could work better to facilitate a more responsive housing market.*

The Henry Review was the most recent comprehensive taxation review, and included consideration of housing affordability and of those taxation treatments noted by the Productivity Commission. On the issue of housing affordability, Henry made the following observations:

[1] Productivity Commission 2004, First Home Ownership, Report no. 28, Melbourne

While high prices or rents may result from increases in housing demand, they can only be sustained at high levels when supply is not responsive. Evidence suggests that the current supply of housing is insufficient, placing ongoing pressure on house prices.

Reforms to stamp duties and land tax would reduce current impediments to housing supply generated by the tax system. However, as taxation is not the major source of supply constraints in the Australian housing market, housing affordability would be best promoted through wider reforms that facilitate housing supply.

Housing supply can be restricted through a range of policies, such as planning and zoning regulations, as well as the approvals processes that govern them. However, such policies are designed to achieve a range of policy objectives, against which their impact on the price of housing should be assessed. The use of infrastructure charges has the potential to improve the allocation of infrastructure. However, where they are not set appropriately, infrastructure charges can reduce the supply of new housing, which can increase overall house prices.

This is not a straightforward area of policy because while reforms to increase supply may promote housing affordability, they can also reduce existing home values and change the shape of Australian cities in ways that many existing residents do not desire. This suggests a serious community dialogue is needed on the distribution and quality of housing across Australia. As a first step, the Council of Australian Governments should review building and land use policies and infrastructure charges to ensure they do not unnecessarily restrict the supply of housing.

Indeed, the recommendations resulting from the Henry Review around housing affordability concentrated on supply-side issues[2]. In particular, under the heading of Housing Affordability the following two recommendations were made:

Recommendation 69: COAG should place priority on a review of institutional arrangements (including administration) to ensure zoning and planning do not unnecessarily inhibit housing supply and housing affordability.

Recommendation 70: COAG should review infrastructure charges (sometimes called developer charges) to ensure they appropriately price infrastructure provided in housing developments. In particular, the review should establish practical means to ensure that these changes are set appropriately to reflect the avoidable costs of development, necessary steps to improve the transparency of charging and any consequential reductions in regulations.

22

4 Consultation with industry

To compliment the modelling approach Master Builders Australia consulted directly with their state and territory counterparts to determine the issues that are most binding in their respective state/territory housing markets.

Consultations focussed on supply-side issues, and specifically on issues which can be addressed through the implementation of a financial incentives agreement between the Commonwealth and state/territory governments. A number of challenges, such as rising developer/infrastructure charges, were a consistent theme across most jurisdictions, while other issues, such as the cost of compliance during the build phase of a new housing development were found to be more pressing in some jurisdictions than in others.

Given these observed inconsistencies it is important that Federal Government policy is flexible and able to be tailored and targeted at the most significant issues which limit new housing supply across the different housing markets in Australia.

A number of issues were raised consistently across housing markets in Australia, including:

- **Inadequate land supply** – this is a result of land release which is either too slow or not adequate to satisfy demand in locations where people want to live – often as a result of long lead times in planning and development or from delays during this process. This was identified either as a top or high priority in each of the states and territories, with New South Wales, Victoria, Queensland, Tasmania and the Australian Capital Territory all identifying this as a top priority issue impacting members ability to build more new homes;
- **Embedded land costs** – This is a broad category which captures all the regulatory costs which are fed into the price of a new block of land before it can be available for sale. Importantly, this encompasses regulatory charges, approval waiting periods, compliance cost and headworks fees, and was nearly uniformly identified as a top priority issue (if not the top priority issues);
- **Infrastructure and developer charges** – This was again nearly uniformly identified as a top priority issue, with the exception of Queensland and South Australia where it was identified as a high priority issue. Although these charges act to push up the price of land during the development phase, similar to the factors included in the embedded land cost above, infrastructure charges are identified separately as they are regularly charged on top of the price of land and in some cases have grown much faster than other regulatory taxes and charges. Additionally, these charges are often seen to not be representative of the amenity of a new residential development, and subject to infrastructure gold plating. However, given the impact of these charges are largely the same as those embedded in the price of land, subsequent scenario chapters in this report model the impact of these charges together with broader embedded land costs; and

- **Poor planning and zoning** – this includes planning and zoning restrictions which limit the type of housing which can be built, inadequate or inflexible zoning which prevents people from living where they want to live, zoning which prevents densification in inner city residential areas, and inadequate forward planning at a local government level. This was identified in New South Wales, Victoria, Queensland, Western Australia and the Northern Territory as top priority impediments to the construction of more new homes.

Meanwhile, a number of other issues were raised as top or high priorities in some States/Territories but not in others. These include:

- **Red and green tape** – this is a broad category which included waiting periods and administrative costs associated with development approvals, building and design approvals, environmental assessments, mitigation costs and expert reporting. New South Wales, Victoria, Tasmania and the Norther Territory all identified growing red and green tape as a top priority to address;
- **Compliance costs** – this includes costs accrued during the build phase for compliance such as the cost of certification of design and construction, compliance to the National Construction Code and meeting energy efficiency standards. Tasmania and the Northern Territory identified this as a top priority; and
- **Inflexible planning schemes** – a number of residential builders noted a lack of flexibility when planning schemes do exist. Planning documents often creates rigidity in the allocation of land for different purposes. These documents often have a long outlook, which is needed to provide long term certainly for investors and developers, but the demand for land can change more quickly and planning regimes which do not allow for flexibility can cause land to be allocated inefficiently. The Northern Territory identified inflexible planning schemes as a top priority, while New South Wales, Victoria and Tasmania also all identified this as a high priority for reform.

A number of other issues were identified less frequently during the consultation process, often as a result of differences in state/territory policy. For example, transaction taxes and land taxes were identified as a high priority for the Australian Capital Territory and New South Wales, but not in other states/territories. A full list of all the issues raised during the consultation process can be found in the table in Appendix A of this report.

The consultation process was undertaken to inform the examination of the potential impacts of reform in the following scenario chapters. Feedback from this process was used primarily as part of the selection criteria in developing the scope of the modelling and the issues to be examined under each scenario. Feedback has also been incorporated into the assessment of the modelling results and to better tailor the modelling framework across the different reform scenarios. In doing so the consultation process provided a qualitative examination which was used to enrich the quantitative outcomes of the modelling.

Importantly, whilst the consultation process identified a number of consistent issues facing housing markets across Australia, it also highlighted a number of different challenges, and perhaps more importantly, the need for Federal Government policy to be flexible and able to be tailored to best target the areas of highest priority across the different housing market in Australia.

5 The impacts of supply side reform

Constraints in the supply side of housing markets have been identified through a number of key public sector inquiries including by the Productivity Commission and the Federal Treasury as a key contributor to sustained high house prices and rents. With these lessons in mind, in this section we have tested the housing market and demonstrated the macroeconomic impacts of changes in supply side and city structure policies.

In the Reserve Bank of Australia research discussion paper *Urban Structure and Housing Prices: Some Evidence from Australian Cities*" (Kulish, Richards and Gillitzer, RDP 2011-03) the impacts of supply side reforms on a stylised major Australian city are demonstrated.

The quantification of the impacts of supply side scenarios in this report builds on the work the previous Reserve Bank research, in particular through:

- adjusting the housing market model for representative small, medium and large Australian cities, allowing for differential impacts by city size;
- using the distribution of city sizes across the states and territories to estimate aggregate impacts by state and territories, and
- using a Computable General Equilibrium model to assess the broader economic consequences.

5.1 Modelling methodology

To capture the specifics circumstances of different markets across Australia we have assessed the potential impacts of each policy on small, medium and large cities. The extent to which each particular supply side constraint is binding in different cities across Australia has been informed through direct consultation by Master Builders Australia with state and territory members.

Quantification of the impacts is undertaken using a combination of the Alonso-Muth-Mills model, and the CEGEM model, Cadence Economics' in-house computable general equilibrium (CGE) model. The use of each of these models is notable, in that the Alonso-Muth-Mills model has been used by the RBA in a working paper assessment of the impacts of supply side restrictions, while CGE models have been widely used by Australian governments at the state and federal levels to assess the impacts of (for example) trade liberalisation, climate change, and housing policy impacts. A more detailed description of the modelling frameworks applied is presented in Appendix B and C.

While the stylised impacts of housing market supply side constraints are valuable, the degree to which different supply side issues are binding varies between different Australian cities owing to differences such as city size and the local planning and government environment. With this in mind, the first step in the quantification process is an assessment the impact of different supply side constraints across the states and territories.

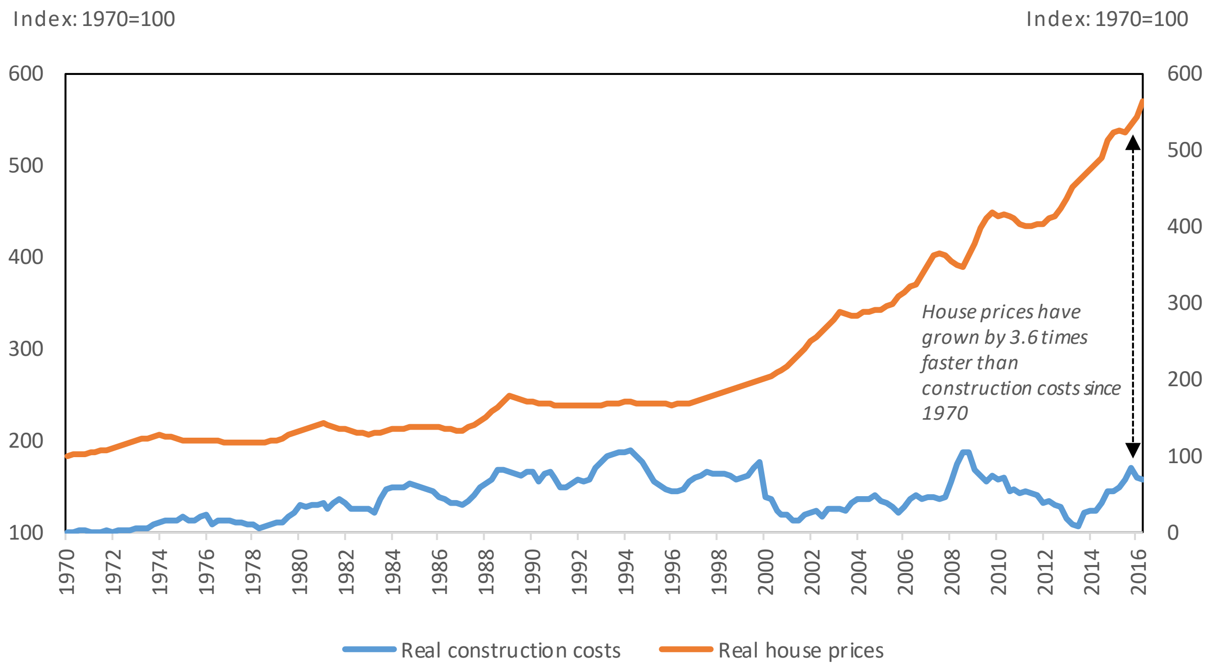
5.2 Developer charges and planning delays

A significant contributor to the cost of new housing developments comes in the form of charges levied on new land developments for utility, transport, communication and other supporting infrastructure.

Additionally, embedded land costs, including land shortages caused by inadequate land release policies, as well as other inputs costs, such as specification costs, holding costs, head works fees and waiting periods all contribute to increasing the costs of development of new residential land. Whilst a detailed assessment of the cost impacts of these embedded costs is unavailable - made more difficult by the need to exclude the market impacts on price and differences across jurisdictions - there is evidence through policy documentation and consultation with industry that embedded costs during the development phase of residential land make a significant contribution to the end price paid for land.

A number of these costs, particularly for the development of supporting infrastructure, have been traditionally paid for by Governments. However, these charges are now largely passed onto new perspective home owners. As a result, land prices have grown by a rate almost four times faster than the cost of construction, as shown in Figure 4. In turn, growth in the price of land has been the single biggest contributor to the rising costs of new housing developments.

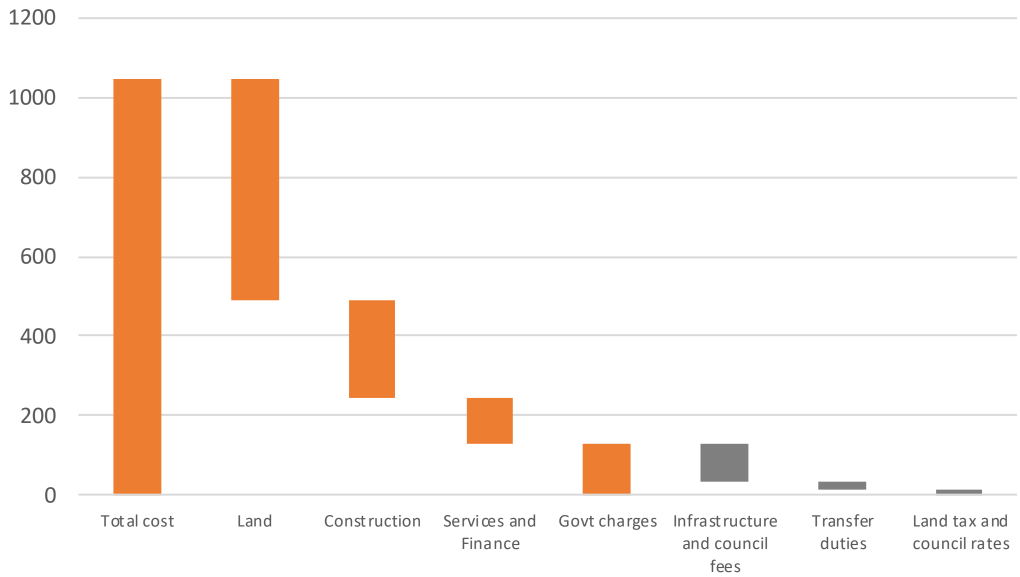
Figure 4: Real construction cost and house prices indexes



Source: Master Builders Australia estimates

In Sydney for example, infrastructure charges can exceed $100,000 and account for more than 10% of the cost of a greenfield new house development[3]. Meanwhile, embedded land costs can add up to well over $300,000, when the impacts of regulated shortages and all other associated cost are accrued. Combined, these costs can add up to well over half of the costs of a newly developed residential lot in Sydney, shown in Figure 5 below.

Figure 5: Development input costs ($ '000), Sydney greenfield development



Source: Master Builders Australia estimates

The impacts of costs incurred during the development phase of new residential land on the structure of a city are heavily dependent on the geographical incidence of the charges. A uniform increase in land costs (either monetary or non-monetary – for example, delays in the release of new land) increases housing prices across a city. It also acts to reduce consumer surplus in the housing market by making living costs more expensive.

The economic impacts

Monetary and regulatory costs related to land development are consistently identified as one of the most pressing deterrents to new dwelling construction and was raised as a priority issues to overcome to boost new housing supply in all capital city housing markets in Australia. Two key issues raised during the consultation in relation to imposing higher costs for housing were developer charges and planning delays (which cause land supply to be inadequate).

The exact impost of developer charges is difficult to determine with large variance in the mix of charges levied across states and councils. In Sydney, it is estimated that government infrastructure charges alone contribute 12% to the cost of a greenfield new housing

[3] Master Builders Australia analysis

development and 5% to an infill two bedroom apartment. The average increase in new housing and infill two bedroom apartment costs across Sydney, Melbourne, Brisbane and Perth is 7% and 4% respectively.

Planning delays impose an opportunity cost on development, tying up otherwise productive capital, with a conservatively short delay of a month imposing a 0.8% opportunity cost under current developer margins. By way of comparison, in the RBA paper *Supply-side Issues in the Housing Sector* it is suggested that precinct planning in Melbourne and Adelaide targeted at improving clarity on permissible developments has taken up to six months off the time required to bring new land to market.[4]

To test the impact of a reduction in the cost of developing new residential land, either through a reduction in developer charges or through embedded costs owing to planning delays, we assume that governments are able to directly reduce the cost of housing through lower (implicit) taxes.

The results of this analysis are presented in Table 1, and can be interpreted in two ways. First, as a scenario that considers only a reduction in developer charges. In this case, it is assumed that developer charges are reduced by around $500 million per annum on new housing, and that planning times are unchanged. This reduction in developer charges ***only*** effectively reduces house prices by around 0.5 per cent on average. This is a fraction of the estimated contribution of developer charges to the cost of new housing discussed above.

Second, in terms of planning delays, the results reflect a reduction in planning and regulatory development timeframes ***only*** by a month, leaving all other existing explicit charges in place. The scenario assumes that 50% of the delay is able to be removed in the first year, with the remaining 50% removed in the second year of the scenario.

[4] Hsieh, Norman & Orsmon, Supply-side Issues in the Housing Sector, *RBA Bulletin, September 2012*

Table 1: Impacts of reduced developer charges or planning delays

	NPV/average	2017/18	2018/19	2019/20	2020/21
GDP ($m)	851	107	251	312	363
Household consumption ($m)	1,400	243	486	477	470
Employment (FTE)	1,216	714	1,417	1,379	1,353
Investment ($m)	2,934	604	1,123	945	808
Construction activity ($m)	1,955	400	746	631	543
Construction jobs (FTE)	2,193	1,537	2,837	2,376	2,022
Dwelling completions		15,820	32,985	34,584	36,074
NSW		*4,978*	*10,380*	*10,883*	*11,352*
VIC		*4,094*	*8,536*	*8,950*	*9,336*
QLD		*3,128*	*6,522*	*6,838*	*7,133*
SA		*1,069*	*2,229*	*2,337*	*2,438*
WA		*1,778*	*3,706*	*3,886*	*4,053*
Tas, NT, ACT		*773*	*1,611*	*1,689*	*1,762*

Source: Cadence Economics Estimates

Notes: All figures are shown as deviations from a counterfactual baseline. NPVs calculated using a 7% discount rate

The economic benefits of either reductions in developer charges or planning delays are compelling. As shown in this stylised and conservative estimate has the potential to add $850 million to GDP and $1.4 billion to household consumption in net present value terms over four years, bringing forward the construction of approximately 36,000 dwellings over this period.

When considering the case for reductions in unnecessary delays in the planning process, the case for reform is particularly compelling as it comes with no first-round reduction in public sector revenues, and indeed would likely increase government revenues in line with increased activity.

Finally, while for some development types and some areas a one month improvement may not be possible, this scenario leaves available other alternate improvements including reductions in other regulatory costs in the development of new residential land.

5.3 The impacts of zoning restrictions

Zoning in cities can place significant constraints on the achievable population density, particularly in inner city areas where the cost of travel is the lowest and desire to live is highest.

Policies to limit housing density (such as building height or plot ratio restrictions) reduce the supply of housing to people in those areas, placing upwards pressure on housing prices in inner city regions and shifting the population further towards the urban fringe.

This shift outwards has two impacts – in the first instance, it increases the level of urban density in the mid and outer city regions. In the second instance, the inner city supply restriction and the shift outwards of the population increases house prices across the entire city, both due to the supply constraint in the inner city and due to the demand increase in the mid to outer city region.

While there are a range of good reasons for imposing zoning restrictions, the potential for significant welfare costs to householders must be considered against the intended amenity (benefits). For example, the RBA discussion paper *Urban Structure and Housing Prices: Some Evidence from Australian Cities* finds that in a city of two million people, relaxation of height constraints by one story decreases house prices near the CBD by around 10%, increasing to a 13% reduction for a city of four million persons.

The economic impacts

The true extent of the direct impact of zoning restrictions is both difficult to measure, in part because the nature of zoning varies greatly from city to city, and the extent to which it distorts housing markets will vary within and between cities. Notably, there are often good reasons for city zoning restrictions. However it is not within the scope or intentions of this report to identify or examine the justifications for zoning restrictions.

To provide a stylised economic impact of reduced zoning impediments, we have drawn on the feedback provided through Master Builders Australia consultation with members. In particular, we are interested in the distribution of how zoning impediments are experienced in cities of different sizes. Zoning restrictions are often most binding in larger cities where the financial incentives for building to (for example) high plot ratios and multiple stories are the highest.

To illustrate this differentiated impact by city size we consider comparable zoning restrictions between large, medium and small cities. In a large city this decreases housing prices per square metre by 2.31%. By comparison, in a medium city this same shock leads to a 1.47% decrease, while in a small city the impact is 0.53%.

Finally, planning restrictions such as height or density restrictions are not generally uniformly binding across a city, with the impost likely to be experienced in high growth pockets.

Acknowledging this we assume that relaxation of planning restrictions impacts only a subset of the geographical area of our representative cities, being 25% of total large city area, 10% of total medium city area and 5% of total small city area. We further assume that any relaxation in planning restrictions takes a four year period to be phased in.

Even with these assumptions the potential impacts are significant, with a net present value of household consumption of over $500 million and an additional 20,000 dwellings estimated.

Table 2: Impacts of zoning restriction removal

	NPV/average	2017/18	2018/19	2019/20	2020/21
GDP ($m)	323	30	71	120	176
Household consumption ($m)	564	69	137	206	277
Employment (FTE)	498	202	400	597	793
Investment ($m)	1,226	171	317	445	559
Construction activity ($m)	816	113	211	296	373
Construction jobs (FTE)	935	434	800	1,114	1,390
Dwelling completions		4,472	9,312	14,513	20,076
NSW		*1,673*	*3,483*	*5,428*	*7,509*
VIC		*1,408*	*2,933*	*4,571*	*6,323*
QLD		*619*	*1,289*	*2,009*	*2,778*
SA		*258*	*538*	*838*	*1,159*
WA		*395*	*822*	*1,281*	*1,772*
Tas, NT, ACT		*119*	*248*	*387*	*535*

Source: Cadence Economics Estimates

Notes: All figures are shown as deviations from a counterfactual baseline. NPVs calculated using a 7% discount rate

5.4 The impact of transportation costs

Announced in the 2017-18 Federal budget was a range of measures intended to improve housing and transport related infrastructure, including the $1 billion National Housing Infrastructure Facility, and $75 billion from 2017-18 to 2026-27 for critical road, rail and airport infrastructure.

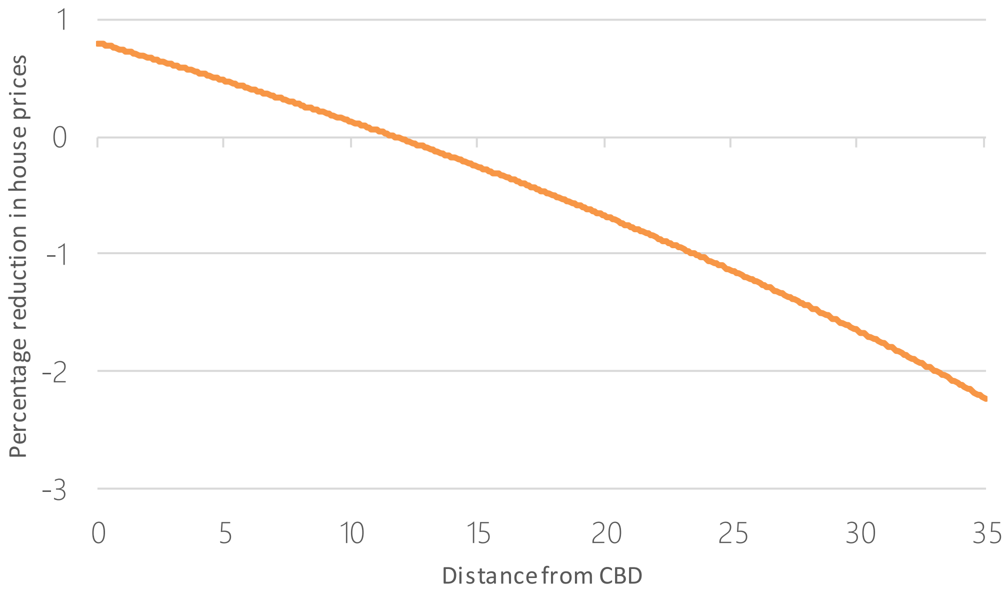
This scenario builds on a previous piece of work by Cadence Economics, commissioned by Master Builders, which examined the contribution of the Federal Governments Infrastructure spending package announced in the 2017 Federal Budget. The subsequent analysis makes an additional contribution by assessing the impact of improvements in transport links to the housing sector of cities of different sizes and across each state/territory in Australia.

The costs of transport are a significant component of household expenditure in cities. The cost of travelling between a place of residence and place of work is a major factor in deciding where to live – for example, near the CBD (or nodes on transport networks) the price of housing will be high, however the cost of transport will be low, while at the urban fringe the opposite holds.

Targeted investment in transport infrastructure can help to reduce transport costs through, for example, reducing road congestion or increasing carrying capacity and reach of rail and other public transport networks. This downward pressure on the cost of transport improves the viability of living further from work, allowing more of the population to live further from the CBD and in turn reducing price pressure for housing closer to the CBD.

The shift in demand to outer city regions increases prices in outer regions as shown in Figure 6. This increase however is more than offset by the reduction in travel costs, and a reduction in house prices in the inner city regions leaving a net welfare increase for households across the city. Better transport infrastructure also places implicit downward pressure on future house prices by way of greater supply of well-located residential land.

Figure 6: House price reductions due to 1% transport cost reduction in a large city



Source: Cadence Economics Estimates

The economic impacts

To measure the impacts on housing prices and production of these combined announced measures, we must first assess the likely proportion of that commitment that will go to reducing the cost of private transport, and of that proportion what the reduction in travel costs might be. With the detail of how the identified money is to be spent yet to be completed, we must rely on alternate data sources to compile a defensible scenario.

Infrastructure Australia publishes the Infrastructure Priority List, both summarising and prioritising the major infrastructure investments at the state, territory, and national levels – many of which pertain to transport infrastructure.

The detailed business cases are not published by Infrastructure Australia, who instead publish brief summaries. For many projects, however, the business cases are published in redacted form, and we are able to determine the approximate proportion of expenditure on major transport projects that goes to improving the efficiency of private transport, and what level of expenditure is required to reduce the average cost of transport in a major city by a given amount.

Using the detail provided in the cost benefit analyses undertaken for the M4, WestConnex and Melbourne Metro we estimate that private transport benefits account for 24% of the total transport benefits of a representative transport infrastructure project, with an investment of approximately $254 million required to reduce the average travel cost per km by 1%. This figure is calculated using only the benefits of major transportation projects that accrue to private road vehicle usage, noting that there are a range of benefits that extend (for example) to freight and business transport that have not been included in this modelling.

The exact pattern of infrastructure expenditure resulting from budget measures is in most cases unreported or as yet unknown. For the purposes of this analysis we assume that fifty percent of the $1 billion National Housing Infrastructure Facility is used on transportation projects, and from the funding allocated to support state infrastructure projects we assume only the Roads to Recovery and fifty percent of the Road component of the Infrastructure Investment Program contributes to reduced travel time for householders.

Using these ratios and the stated Budget numbers above allows us to calibrate shocks for the Alonso-Muth-Mills model and subsequently for the CEGEM model to determine the likely macroeconomic impacts, as shown in Table 3. The impacts of the budget measures make a $1.15 billion contribution to aggregate household consumption, and add approximately 38,000 houses to the national housing stock.

Table 3: Impacts of 2017-18 budget measures to increase transport infrastructure

	NPV/average	2017/18	2018/19	2019/20	2020/21
GDP ($m)	688	83	167	270	319
Household consumption ($m)	1,145	182	309	436	457
Employment (FTE)	998	535	897	1,254	1,305
Investment ($m)	2,418	449	693	899	864
Construction activity ($m)	1,611	297	461	599	578
Construction jobs (FTE)	1,823	1,142	1,751	2,253	2,146
Dwelling completions		11,972	22,468	32,290	38,368
NSW		*3,882*	*7,285*	*10,470*	*12,441*
VIC		*3,167*	*5,943*	*8,541*	*10,148*
QLD		*2,252*	*4,226*	*6,074*	*7,217*
SA		*825*	*1,548*	*2,224*	*2,643*
WA		*1,330*	*2,497*	*3,588*	*4,264*
Tas, NT, ACT		*516*	*969*	*1,393*	*1,655*

Source: Cadence Economics Estimates

Notes: All figures are shown as deviations from a counterfactual baseline. NPVs calculated using a 7% discount rate.

Appendix A: State/Territory Housing Affordability Priorities Table

The following table outlines the key priorities raised in the industry consultation process.

Housing Affordability Top Priorities - what prevents you from building more new homes

	NSW	VIC	QLD	SA	WA	TAS	NT	ACT
Land supply - inadequate supply of land by government	✔	✔	✔	✓	✓	✔	✓	✔
Embedded land costs	✔	✔	✓	✔	✔	✔	✔	✔
Infrastructure/Developer charges	✔	✔	✓	✓	✔	✔	✔	✔
Poor planning and zoning	✔	✔	✔		✔		✔	
Red and green tape	✔	✔				✔	✔	
Complaince costs - building phase	✓		✓			✔	✔	✓
Finance - availability and cost				✓				
Material costs and availability				✓		✓	✓	
Workplace health and safety requirements						✓	✓	
Transaction taxes and land taxes	✓							✓
Tax deductibility - capital gains tax and negative gearing						✓		
Inflexible planning schemes	✓	✓				✓	✔	
National Construction Code (NCC) - energy efficiency standards and engineering design requirments						✓		
Inconsistencies in valuations			✔			✓		

✔ Top Priority

✓ High Priority

Appendix B: Modelling details

The analysis undertaken in this report relies on a combination of two separate models. The first is the Alonso-Muth-Mills model of housing for a monocentric city, used to estimate the impacts of each of the policies on city structure and the details the housing market.

The version of this model used for this analysis is adapted from the Reserve Bank of Australia's research discussion paper "*Urban Structure and Housing Prices: Some Evidence from Australian Cities*" (Kulish, Richards and Gillitzer, RDP 2011-03). The functional structure of the model is unchanged from that used by Kulish, Richards and Gillitzer, with a detailed description of the model provided in Appendix A of that paper.

The Alonso-Muth-Mills model is implemented in Python, with results validated against the Mathematica code as used by Kulish, Richards and Gillitzer. We have calibrated the model to provide insight into the impacts of different supply side policies against three different size Australian cities – a large city representing cities of the size of Sydney and Melbourne, a medium city for those of sizes between Brisbane and Wollongong, and a small city for anything smaller.

Calibration of the impacts of transport infrastructure investments feeding into the Alonso-Muth-Mills model was done using the assistance of key business cases from the Infrastructure Australia priority list as at February 2017. In particular the business cases for the M4, WestConnex and the Melbourne Metro provide detail on the level of travel benefits resulting from large scale transport infrastructure spending. Importantly, only the private travel benefits have been used from these business cases when calibrating the policy scenarios.

The second model used is the CEGEM model, Cadence Economics' in-house Computable General Equilibrium (CGE) model. CGE models are widely used and accepted within the Australian policy debate, including having been applied by Australian governments at the state and federal levels for policy issues including the impacts of trade liberalisation, carbon pricing and taxation efficiency analysis.

The CEGEM model is used to estimate the indirect and economy wide impacts of the specific housing market impacts revealed by the Alonso-Muth-Mills model. Specifically, the Alonso-Muth-Mills model provides impacts on the cost of housing under different policy settings, which is used as an input to shock the CEGEM model. The CEGEM model in turn provides insight into changes in economic aggregates including GDP, household consumption, demand for housing and construction sector activity.

The CEGEM model is in the broad class of GTAP/GTEM models, and is solved year-on-year in a recursive dynamic structure. To account for the comparative static nature of the Alonso-Muth-Mills model we assume a seven year transition path for any price changes used to shock the CEGEM model.

Appendix C: The CEGEM model – additional detail

CEGEM is a multi-commodity, multi-region, dynamic model of the world economy. Like all economic models, CEGEM is a based on a range of assumptions, parameters and data that constitute an approximation to the working structure of an economy. Its construction has drawn on the key features of other economic models such as the global economic framework underpinning models such as GTAP and GTEM, with state and regional modelling frameworks such as Monash-MMRF and TERM.

Labour, capital, land and a natural resource comprise the four factors of production. On a year-by-year basis, capital and labour are mobile between sectors, while land is mobile across agriculture. The natural resource is specific to mining and is not mobile. A representative household in each region owns all factors of production. This representative household receives all factor payments, tax revenue and interregional transfers. The household also determines the allocation of income between household consumption, government consumption and savings.

Capital in each region of the model accumulates by investment less depreciation in each period. Capital is mobile internationally in CEGEM where global investment equals global savings. Global savings are made available to invest across regions. Rates of return can differ to reflect region specific differences in risk premiums.

The model assumes regional labour markets operate in a model where employment and wages adjust in each year so that, for example, in the case of an increase in the demand for labour, the real wage rate increases in proportion to the increase in employment from its base case forecast level. The coefficient of adjustment is chosen so that the employment effects of a shock are largely eliminated after about ten years. Labour supply is determined by demographic factors.

CEGEM determines regional supplies and demands of commodities through optimising behaviour of agents in perfectly competitive markets using constant returns to scale technologies. Under these assumptions, prices are set to cover costs and firms earn zero pure profits, with all returns paid to primary factors. This implies that changes in output prices are determined by changes in input prices of materials and primary factors.

The advantage of a global model such as CEGEM is that it accounts for bilateral trade flows of all commodities between regions. Goods are imperfect substitutes, implemented through the Armington assumption. The model does not require the regional current account to be in balance as the capital account can adjust to maintain balance of payments equilibrium.

Base data

The starting point for the base data in CEGEM is the global database produced by the Global Trade Analysis Project (GTAP). This database is comprised of 140 country and regional groups and 57 production sectors. The Australian component of this database was supplied by the Productivity Commission, and is based on Australian input-output tables produced by the Australian Bureau of Statistics (ABS).

Dynamics

CEGEM is a recursive dynamic model that solves year-on-year over a specified timeframe. The model is then used to project the relationship between variables under different scenarios, or states, over a predefined period. This is illustrated in Figure A1. This shows the reference case scenario forms the basis of the analysis. The model is solved year-by-year from time 0, which reflects the base year of the model, to a predetermined end year (in this case 2030).

The variable represented on the vertical axis of Figure A1 could be one of the hundreds of thousands represented in the model ranging from macroeconomic indicators such as real GRP to sectoral variables such as the exports of thermal coal. In the figure, the percentage changes in the variables have been converted to an index (= 1.0 in 2005) and are projected to increase by 2030.

Set against the reference case scenario is a 'scenario projection'. This scenario represents the impacts of imposing a policy shock. That results in a new projection of the path of the variable over the simulation time period. The impacts of the policy change are reflected in the differences in the variable at time T. It is important to note that the differences between the reference case and policy intervention scenario are tracked over the entire timeframe of the simulation.

Figure A1: Dynamic simulation using CEGEM