

Using land for housing

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This *Cut to the Chase* summarises the Commission's report on using land for housing.

The inquiry

The Government asked the Productivity Commission to look into the processes that New Zealand's fastest-growing local councils use to provide land for housing. These include planning, zoning and the provision of infrastructure such as roads, parks and water pipes. In investigating these issues, the Commission focused on ten high growth areas (Whangarei, Auckland, Tauranga, Hamilton, Waikato, Wellington, Christchurch, Selwyn, Waimakariri and Queenstown Lakes) and sought evidence from a number of countries.

The need for more land and more opportunities to develop housing

House prices have risen dramatically over the past fifteen years. A major contributor to this price growth has been an insufficient supply of land that is ready for housing, both within cities (brownfield land) and outside of them (greenfield land). Evidence of this shortfall can be seen in the rising price of urban land. Land now makes up 50% of the total value of a property in many high-growth New Zealand cities and around 60% of the value of an Auckland property.

The effects of not enough land

The most obvious effect of not enough land is a shortfall of housing and rising house prices. This is being seen most dramatically in Auckland.

A shortage of developable land limits housing choices for renters and buyers. When combined with restrictive planning rules, high land prices encourage developers to build more expensive dwellings. The shift towards more expensive housing, and the resulting decline in the construction of lower-cost dwellings has a number of harmful social impacts, including housing costs which are among the highest in the OECD, household crowding, barriers to wealth accumulation, and limits on the ability of people to move to areas with more jobs and higher incomes. Central government bears many of the costs and risks created by these harmful impacts, including through higher rental subsidy payments and higher health spending.

An inadequate supply of land for housing also creates a vicious cycle, whereby landowners see more benefit in holding on to undeveloped sections to earn capital gains, instead of releasing it for housing. This adds to the upward pressure on land – and house – prices.

What is causing this shortfall?

Costly rules and restrictions

There are a number of rules and regulations in the planning system that increase the cost of new housing, make it harder to build lower-cost dwellings, and that restrict the supply of land by limiting the ability of cities to grow up and out. In some cases, these rules create costs that exceed their likely benefits. Examples include minimum apartment size rules and balcony requirements, minimum parking requirements and density limits. Some rules could potentially be beneficial, but are badly designed. Others seem to go way beyond what is needed to ensure a well-functioning city.

Insufficiently responsive infrastructure provision

In order to become ready for development, land needs to be both zoned and serviced with infrastructure. Installing new infrastructure is an expensive exercise, and these costs should be met by those who benefit from the new assets. Yet in some cities, the charges for new infrastructure are set too low, requiring cross-subsidies from existing ratepayers. As a result, local authorities or their infrastructure providers tightly control the supply of new assets, to keep costs and risks down.

A sluggish planning system

The planning system is not adequately responsive to changes in demand. Land price information is a critical indicator of demand pressures, but planners do not take it into account when setting land use controls, planning the future supply of infrastructure, or deciding to release new residential land. Instead, they rely on forecasts of population growth, which may – or may not – match the actual demand of where people want to live. Even where councils do wish to increase capacity in response to higher demand, process requirements in the planning system and the lack of integration between land use, infrastructure and transport planning can make it difficult for local authorities to act promptly and consistently.

Incentives to oppose the growth of cities

Many groups have incentives to oppose growth in their cities. Ratepayers may not want their councils to invest in more infrastructure, because of concerns about higher debt levels or rates bills. Homeowners may oppose more intensive developments near them, because they have concerns about the effects on their house values and on the amenity of their neighbourhoods. And landowners may not welcome larger releases of residential land, where they perceive that a tight supply helps support the price of their properties.

These groups have a disproportionate influence in local council processes, including elections and consultation on budgets and plans. As a result, many council land use rules and policies effectively protect the interest and wealth of those who already own housing, to the detriment of those who do not. Locally-driven planning can deliver decisions that are not in the national interest.

Meeting the demand for land

Increasing the supply of development capacity to meet the demand for housing will require action on a number of fronts. The Commission identified six main areas where there would be benefits in policy change.

Better use of existing assets

There are opportunities to accommodate population growth without building costly new infrastructure, where spare capacity is available in existing assets. However, in order to do this, councils need to have a good understanding of the use and condition of their assets and lift restrictive planning controls where spare capacity exists. Many councils need to improve the quality and use of information about their infrastructure assets.

More and better cost-recovery

Councils need new funding tools, and should make greater use of existing tools, to fund new infrastructure. Wider use by councils of volumetric charging for water would help manage demand and defer costly new asset upgrades. The Government should remove restrictions on councils using tolls and congestion charges to ensure a more efficient roading network.

The costs of installing new infrastructure vary depending on the nature and location of a development, yet some current council development contributions do not reflect these cost differences. In Auckland, the council's water provider charges one flat price, which only recovers two-thirds of the cost of installation. Councils and their providers should set infrastructure prices to more accurately reflect costs, as this would enable more land to be unlocked, increasing competition between landowners, and putting downward pressure on land prices

Some members of the community benefit more from the installation of new infrastructure, but under current practice, the costs of these assets are spread across the city through general rates. There is potential to make more use of targeted rates, so that those who directly benefit pay for them over time.

The current exemption on central government paying rates on the land it owns in cities should be removed. This will discourage the Crown from holding on to land it no longer requires and instead release it for higher-value uses, such as housing.

Proper cost-benefit analysis for land use rules

Too many land use regulations are approved on the basis of poor or incomplete analysis. Greater use of cost-benefit analysis is needed to reveal the full costs and benefits of proposed new rules, and to identify who wins and who loses from their introduction. This will help make clear when proposed new rules actually benefit the wider community, rather than narrow, vested interests.

A deeper review of the planning system

The current planning system is not fit for purpose. The legislative framework makes it hard to integrate decisions about land use, transport and infrastructure provision, and does not give sufficient attention to the needs of cities and housing. The system is also slow to respond to increases in the demand for space, and has expanded to cover issues that are arguably best left for individuals to decide.

The Commission has recommended a number of smaller improvements to the planning system, and the Government has recently announced a package of reforms aimed at giving more weight to housing and speeding up approvals. These will help resolve some of the problems with the current frameworks, but if New Zealand is to see significantly better performance from its planning system, a deeper review is needed.

More help for councils to deliver dwellings

Councils in our faster-growing cities have a clear idea about how they want to develop in the future, and how they intend to meet a growing population's demand for housing. For our larger cities, this typically involves growing through more intensive development, rather than building outward. To achieve this goal, councils need to tackle the tensions between the interests of existing residents and the more flexible rules that will be required to accommodate new residents.

Some cities are responding to this challenge by establishing urban development authorities that can redevelop inner city sites to deliver large numbers of new dwellings. The Government should support these efforts, including by providing streamlined planning processes, and granting local UDAs powers of compulsory acquisition in certain circumstances.

A credible commitment to release land and control land price inflation

However, if councils are unable to deliver a sufficient supply of development capacity to meet housing demand, then central government should step in to ensure this occurs.

The best measure of whether demand is being met is the difference in price between urban land that can be developed, and land that cannot. In Auckland, residential land is more than nine times more expensive than other land and this gap is increasing. The Government should set a threshold beyond which it will require councils to release and service more land. Setting a credible commitment that land prices will not increase beyond a certain level will discourage land banking, by removing expectations of ongoing future capital gains. It will also encourage councils to ease planning controls in the inner city, if they want more intensive development.

Providing greater balance between local and national interests

At the heart of the Commission's recommendations is the idea that greater balance is needed between local and national interests in the planning system. The growth of cities has benefits for the whole country, such as higher national productivity and greater wellbeing. Yet decisions about the pace and scale of city growth are taken locally, creating social, economic and fiscal costs that are ultimately borne by central government. The planning system needs to recognise that both central and local governments have an interest in the growth of cities, and ensure prompt and credible responses to increases in the demand for housing.

The full report *Using land for housing* is available at www.productivity.govt.nz.

The **New Zealand Productivity Commission** – an independent Crown entity – conducts in-depth inquiries on topics selected by the Government, carries out productivity-related research, and promotes understanding of productivity issues.