SUBMISSION TO THE PRODUCTIVITY COMMISSION INQUIRY ON PUBLIC INFRASTRUCTURE

PREPARED BY

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DECEMBER 2013

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1 About UDIA

The Urban Development Institute of Australia (UDIA) is the peak body representing the property development industry throughout Australia.

UDIA aims to secure the economic prosperity and future of the development industry in Australia, recognising that national prosperity is dependent on our success in housing our communities and building and rebuilding cities for future generations.

The development industry is an essential cornerstone of the Australian economy. Construction alone contributes

In 2010, UDIA, on behalf of its members, commissioned Property Insights to undertake an economic impact study of the property development industry in Australia. The study confirmed the sector's significant influence on the Australian economy, as evidenced by the below findings:

- The property development industry is the fourth largest industry in Australia in terms of its contribution to GDP. It directly accounts for 7.3% of GDP and, taking into account indirect impacts on the rest of the economy, delivers an additional 6.2% of national output.
- Almost one in ten Australian workers is employed in property development, with the industry directly accounting for over 975,700 jobs (9.1% of the workforce). For comparison, the mining industry employs less than 2% of the workforce. Property development employs a further 749,600 people through its indirect impact on the rest of the economy.
- As a conservative estimate, the property development industry, both directly and through associated industries, generated in excess of $29.7 billion of State and Federal taxes in 2007/08.

2 Introduction

The Urban Development Institute of Australia (UDIA) welcomes the opportunity to provide input into the Productivity Commission's Inquiry into Public Infrastructure.

Effective and efficient infrastructure provides the fundamental framework that allows modern economies to operate. Infrastructure investment has the potential to greatly improve Australia's economic productivity and the quality of life in our cities, and with careful planning and delivery, can generate an enormous positive net benefit for our society.

The timely provision of sufficient major economic infrastructure such as transport and utilities infrastructure is also an ongoing area of concern for the urban development industry. Urban development by its very nature requires large investments in new infrastructure, supporting jobs, businesses, and generating a large proportion of Australia's economic output.

Unfortunately the provision of key economic infrastructure has struggled to keep up with strong growth in the Australian economy and population in recent years, and there is currently a large and growing 'infrastructure gap'. The failure of governments to adequately invest in new and upgraded infrastructure has put substantial strain on existing networks, increasing congestion, dragging on productivity, and putting Australia's economic future at risk.

A lack of key infrastructure necessary for the supply of new housing, and an increasing propensity for governments to front load the cost of infrastructure onto the upfront cost of housing, has both pushed up the cost of new housing and constrained its supply. This has worsened existing problems with housing affordability and added to Australia's already substantial dwelling shortfall.

With Australia's mining investment and commodities boom currently slowing, there will be increased pressure incomes, unemployment and state and federal government budgets. Now, more than ever, greater levels of infrastructure investment will be essential to boost employment, drive productivity, and facilitate growth in the rest of the economy.

3 Recommendations

- The Federal Government should increase its level of debt in order to fund additional urban infrastructure investment.

- The Federal Government should work with State and Local Governments to ensure that where developer contributions are used, they are reasonable, transparent and justified in their implementation, and that there are not more appropriate forms of funding available.

- The Federal Government should play a role in benchmarking housing infrastructure costs around the nation, with a view to reducing those costs.

- Favour funding and financing approaches that spread the cost of infrastructure out over extended time frames, rather than impose it up front, such as through developer contributions.

- Continue to make greater use of public private partnerships.

- Further investigate Tax Increment Financing (TIF) as a means to fund infrastructure investment.

- In instances where privatisation of existing state government assets is in the best interests of consumers and businesses, the Federal Government should incentivise state governments to sell those assets and invest the proceeds in new infrastructure projects.

- Strengthen the role of Infrastructure Australia, and commit to rigorous and comprehensive cost benefit analysis to ensure the greatest value for money on new infrastructure projects.

- Consolidate local infrastructure enabling programs, such as the Housing Affordability Fund and Building Better Regional Cities, in to one major local infrastructure fund, and commit to ongoing and increased funding to such a scheme.

- Ensure that infrastructure funding, financing and implementation strategies are integrated across different functions of government (including land use and transport planning, economic and urban development and environmental assessment), and across different levels of government.

- Investigate ways to remove barriers to private investment in public infrastructure, and improve the attractiveness of public infrastructure as an investment.

- The Federal Government should work with state and territory governments to improve the supply of urban land in Australia's cities.

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4 Guiding Principles

Efficiently and effectively financing, funding and delivering infrastructure is a complex undertaking, with numerous different options and approaches available. UDIA has developed the following guiding principles to provide overarching direction for government decisions on infrastructure.

- Infrastructure funding, financing and delivery decisions should be made with regard to their impact on land and housing affordability.

- Infrastructure financing and funding should take in to account considerations of equity
  - Infrastructure costs should be transparent, reasonable and fairly apportioned between beneficiaries.
  - Infrastructure financing and funding should favour spreading costs out over extended timeframes rather than imposing up front charges or levies.

- Decisions to invest in infrastructure should be transparent and based on economic merit, with rigorous cost benefit analysis for major projects.

- The Government should fund and provide infrastructure in instances where markets and private investment produce unsuitable outcomes. Elsewhere, the Government should encourage and facilitate private investment and market solutions.

- Infrastructure funding, financing and delivery decisions should be made holistically, with coordination between the different tiers of government, and integration with planning systems.

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5 Defining Public Infrastructure

At its most basic level, infrastructure refers to the physical and organisational structures necessary for an organisation to operate effectively. Various terms are used to differentiate between types of infrastructure, including:

- Hard (physical) or soft (institutional/organisational)
- Social or economic infrastructure
- Private or public infrastructure
- National, regional or local infrastructure

The terms of reference for this inquiry limit its scope to 'nationally significant economic infrastructure' and 'major infrastructure projects', which is clearly very broad and context dependent. For the purpose of this enquiry, UDIA considers 'nationally significant economic infrastructure to be infrastructure that has a material impact on national productivity, employment or economic output.

A key characteristic of many of Australia's nationally important infrastructure systems is that they are composed of pieces which are insignificant on their own, but combine to produce economic benefits greater than the sum of their parts. For example, the pit and pipe works to allow individual businesses and households connect to the NBN are not nationally significant individually, but in aggregate, they form a core link in the NBN, a system with the potential to substantially impact on national productivity and economic output.

Similarly, infrastructure such as road, rail, water, drainage, gas, electricity and telecommunications networks must be considered as infrastructure of national economic significance in their entirety.

Whether or not an infrastructure project can be considered to be a 'major' infrastructure project depends very much on the context and scale in consideration. For example, an urban road project may be a major project at a local or regional level, but not at a national level (although it may still be of national economic significance).

The following are examples of what UDIA considers may constitute 'major infrastructure projects' or 'infrastructure of national economic significance' for the purpose of this inquiry.

- Local, regional and national roads
- Urban and national rail systems
- Gas networks
- Stormwater systems
- Telecommunications networks
- Water/waste water networks
- Electricity networks

6 Infrastructure Financing and Funding

Infrastructure funding refers to the revenue-raising sources and streams that are used to pay for the costs of an infrastructure project over its lifetime, whilst infrastructure financing refers to the capital necessary for the upfront construction of infrastructure, and the mechanisms by which that capital is raised.

In the past, infrastructure funding, financing and provision was largely the domain of governments. This had the benefit of helping to ensure that infrastructure was adequately provided and priced where market frameworks for its provision were ineffective, and where infrastructure networks are natural monopolies.

In recent years the role of all levels of government in providing public infrastructure has been steadily contracting. Better market regulation and technological developments have expanded the potential for user charges, reducing the need for governments to own and operate infrastructure, and public private partnerships (PPPs) have also become more prevalent. The privatisation of many government owned enterprises with the responsibility for providing public infrastructure (such as electricity distribution and telecommunications networks), has also seen a growing proportion of infrastructure provided by the private sector.

There are a number of different methods currently employed in Australia to fund and finance infrastructure.

6.1 Government Debt

Federal, State and local Governments take on debt to provide infrastructure, which is then ultimately paid back through taxation or user charges. Governments typically have an advantage in that they can typically borrow on more favourable terms than many other entities, which can make government borrowing for public infrastructure preferable to borrowing by businesses or individuals.

Governments in Australia in recent times have been averse to taking on additional debt loads, despite net government debt levels remaining low. Given the strong positive economic return on efficient and effective infrastructure investment, there is a strong case to be made for increasing government debt, in order to fund Australia's future infrastructure needs. This is especially true for the Federal Government, which has a greater revenue raising ability, and can borrow on more favourable terms than state governments. **The Federal Government should increase its level of debt in order to fund additional urban infrastructure investment.**

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6.2 Developer Contributions

Developer contributions are upfront charges levied on developers for the provision of new or upgraded infrastructure. They typically take the form of infrastructure provided and paid for by the developer, a gift of land from the developer, or a monetary payment made by the developer to the government, ostensibly for the provision of infrastructure.

Developer contributions have gained increasing importance as an infrastructure funding mechanism as a result of:

- Increasing demand for and cost of infrastructure
- Fiscal constraints on local governments as a result of rate capping and reduced grants from state and federal Governments.
- A shift in broader expectations away from government financing and funding of infrastructure toward cost recovery from users/beneficiaries of infrastructure.

Their implementation is justified based on the belief that those who directly benefit from infrastructure should cover the costs of its construction. To be fair and effective, developer contributions should be charged proportionately to the benefit received by the beneficiary of the infrastructure, and should be transparent in their calculation and application. Unfortunately all too often this is not the case and developer contributions are unreasonable and excessive, damaging both business and housing affordability.

Developer contributions are frequently opaque and unjustified in their application, and there may be no clear connection between the cost of the infrastructure provided and the contribution, to the extent that the contribution may be well in excess of the cost of the infrastructure it is supposed to pay for. Additionally in many cases developer contributions are used to pay for infrastructure that benefits the wider community (for example trunk roads and utilities infrastructure upgrades). In this case, developers and ultimately new home buyers are being forced to subsidise the rest of the community.

A further problem with developer contributions is that where the developer is required to build and bear the upfront cost of public infrastructure, local governments and councils have a strong incentive to set unnecessarily high engineering and construction standards in order to minimise their ongoing maintenance and replacement costs. Where these reduced costs aren't reflected in lower council rates, new home buyers effectively end up paying for their infrastructure twice, once through a higher up front house price, and again through recurring rates.

The Federal Government should work with State and Local Governments to ensure that where developer contributions are used, they are reasonable, transparent and justified in their implementation, and that there are not more appropriate forms of funding available.

The Federal Government should also play a role in benchmarking housing infrastructure costs around the nation, with a view to reducing those costs.

It is important to note that whilst developer contributions are nominally paid for by developers, the cost is reflected in the price of new homes, and thus ultimately borne by new home buyers. UDIA estimates that the upfront infrastructure costs imposed on new housing in many instances can be as much as $65,000, which is a considerable proportion of the cost of a new home, and a substantial hurdle for those aspiring to home ownership.

The Federal Government should favour funding and financing approaches that spread the cost of infrastructure out over extended time frames, rather than impose it up front, such as through developer contributions.

6.3 Private Public Partnerships

Private Public Partnerships (PPPs) provide the potential to reduce project costs and construction times, facilitate risk sharing between the public and private sectors, and open up new pathways to private sector financing. PPPs are best suited to large scale infrastructure projects that are large enough, and have a rate of return high enough to make PPPs worthwhile.

There have been several high profile PPP projects in Australia recently that caused significant losses for the private sector party as a result of sub-optimal management and allocation of the risks involved. UDIA believes that problems associated with recent PPP projects can be resolved, and that ultimately PPPs have the potential to be an effective method of financing infrastructure. **The Federal Government should continue make greater use of public private partnerships.**

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7 Alternative Funding and Financing mechanisms

Existing methods of financing and funding infrastructure in Australia may not be sufficient to facilitate the level of infrastructure investment that the Federal Government is looking to undertake. Increasingly governments will have to look to previously unexplored methods of funding and financing infrastructure to meet their infrastructure investment objectives.

7.1 Tax Increment Financing

Investment in new infrastructure by governments increases the amenity of areas with access to the infrastructure, and subsequently the land values of those areas. Tax Increment Financing (TIF) allows governments to capture back some of the value uplift as a result of new infrastructure investment, such as through council rates and other property taxes, and use that to help fund and secure financing for infrastructure investment.

TIF is widely and successfully used in the United States to fund infrastructure, and represents an unrealised opportunity for infrastructure investment in Australia. **The Federal Government should further investigate Tax Increment Financing (TIF) as a means to fund infrastructure investment.**

7.2 Asset Sales

There exists a substantial opportunity to recycle capital from existing government assets into new infrastructure projects. State governments could sell their existing infrastructure assets to the private sector, both freeing up funds and potentially resulting in more efficient use of that infrastructure. Of course privatisation may not be the optimal solution in all instances, and any decision to privatise state infrastructure would have to take in to account the needs of the community, the government revenue lost by selling the asset, and whether sufficient regulation and markets exist to support the asset's privatisation.

In instances where privatisation of existing state government assets is in the best interests of consumers, and businesses, the Federal Government should incentivise state governments to sell those assets and invest the proceeds in new infrastructure projects.

7.3 Increased Retail and Institutional Investment

Another potential way to increase the funds available for infrastructure investment is through increasing access to institutional and retail investors. In particular, Australia's superannuation industry has enormous potential as a source of funding for infrastructure

projects. Methods to unlock investor funds include infrastructure bonds, preferential tax treatment, and addressing existing barriers to investment, such as a lack of market experience in infrastructure investment, concerns over project risk, lack of an established marketplace for infrastructure, and a lack of an ongoing, diversified pipeline of new infrastructure projects.

One specific model advocated by UDIA involves the establishment of an Urban Infrastructure Fund to increase retail and institutional investment. The Fund, which is outlined in the Urban Coalition's Plan, *A New Deal for Urban Australia*, would create a new infrastructure asset class. Returns on this asset class would be credit enhanced via a tax rebate or government guarantee, in order to make it more attractive to investors (see appendix).

Money raised by this investment product would be used by the Urban Infrastructure Fund to provide seed finance to qualifying infrastructure projects, submitted by project sponsors such as local governments, statutory authorities or regional development corporations. Project sponsors would complement seed finance with funding from other sources (such as traditional government recurrent expenditure, PPPs, bank finance, etc.)

The Federal Government should investigate new ways remove barriers to private investment in public infrastructure, and improve the attractiveness of public infrastructure as an investment.

8 Infrastructure Selection, Planning, Provision and Coordination

Whilst productive government investment in infrastructure can deliver enormous net benefits to the Australian economy and broader Australian society, poor investment decisions, where the cost of building infrastructure exceeds the benefit it provides is both economically damaging and a strain on government resources. In the current weak economic climate and constrained budgetary environment, getting the best value for money in new infrastructure investment is critical.

8.1 Infrastructure Australia

Infrastructure Australia was established by the Australian Government to provide objective and independent advice on Australia's future infrastructure needs, and the best way to fund, finance and deliver that infrastructure. The existence of a strong and independent organisation such as Infrastructure Australia, along with thorough cost benefit analysis will help ensure that Australia gets the right infrastructure, and that the Government achieves the greatest value out of its spending on infrastructure investment.

The Federal Government should strengthen the role of Infrastructure Australia, and commit to rigorous and comprehensive cost benefit analysis to ensure the greatest value for money on new infrastructure projects.

8.2 Infrastructure Planning and Coordination

Also critical to the successful implementation of major infrastructure is adequate planning and coordination between the different levels of Government. State and local governments have varying processes established for the selection, planning and implementation of infrastructure, with objectives that may compete or conflict with other areas and levels of government.

To ensure the most efficient, cost effective and timely implementation of major infrastructure, **the Federal Government should ensure that its infrastructure funding, financing and implementation strategies are integrated across different functions of government (including land use and transport planning, economic and urban development and environmental assessment), and across different levels of government.**

8.3 Infrastructure Funding Programs

One of the most effective ways for the Federal Government to achieve its objective of increasing investment in to productivity enhancing economic infrastructure is through specific funds or programs with the purpose of enabling key infrastructure. Two existing programs that UDIA has been very supportive of are the Building Better Regional Cities (BBRC) program and the Housing Affordability Fund (HAF), both of which grant federal funds for the construction of key infrastructure such as roads, telecommunications, and water infrastructure.

The Federal Government should consolidate local infrastructure enabling programs, such as the Housing Affordability Fund and Building Better Regional Cities, in to one major local infrastructure fund, and commit to ongoing and increased funding to such a scheme.

9 Infrastructure Costs

The cost of providing new infrastructure in Australia can be considerably more than the cost to provide similar infrastructure in other developed countries. Whilst much of this disparity can be attributed the generally high cost nature of the Australian economy and peculiarities specific to Australia (e.g. competition for resources from the mining industry), one aspect of particular interest to UDIA is the extremely high cost of urban land in Australia.

Urban land is a key direct input in to infrastructure such as rail and road projects, which can require the acquisition of large corridors of land, often at a very high cost. In some cases, the cost to acquire the necessary corridors for new infrastructure is so prohibitively high that techniques such as extensive underground tunnelling must be employed, also at very high cost.

Even in instances where an infrastructure project doesn't require large quantities of land itself, the high cost of urban land is priced into every other input used in its construction. High land prices are reflected in high housing costs and business rents, which are then reflected in the price of labour, and goods and services provided by businesses. High land prices have an inflationary flow on effect throughout the entire economy, including the construction of infrastructure.

One of the primary causes of high land costs in Australia's major cities is the restrictive planning and land supply policies that have been adopted by many jurisdictions. In the context of rapid population growth, restricting the supply of new urban land on the fringe has the effect of considerably increasing the price of land across a city's urban area. The impact of restrictive planning on land prices is most visible in the difference in prices between land inside and outside of urban growth boundaries, with land inside the growth boundary easily ten or more times the price of similarly located land outside the growth boundary.

Governments should take an interest in addressing the high cost of urban land not only because of its impact on the cost of providing infrastructure, but also for the role that land prices have in determining costs and competitiveness throughout the Australian economy. **The Federal Government should work with state and territory governments to improve the supply of urban land in Australia's cities.**

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10 Concluding Comments

UDIA would like to thank the Productivity commission for the opportunity to provide this submission to the Inquiry into Public Infrastructure. Sufficient and efficient investment in public infrastructure will be critical to improving productivity and economic growth as Australia faces soft economic conditions in the coming years.

UDIA would welcome the opportunity to discuss any aspect of this submission in greater detail. For further information, please contact UDIA National on 02 6230 0255 or at udia@udia.com.au

11 Appendix

Urban Coalition - Urban Infrastructure Fund

> *Recommendation 1*
> *Unlock private sector dollars through a new Urban Infrastructure Fund*

Introduction

This section outlines a model for boosting the capital available to fund local community infrastructure.

It recommends the Australian Government (in collaboration with states and territories) foster an urban infrastructure investment asset class through a new Urban Infrastructure Fund.

This asset class would offer lower risk, credit-enhanced returns that appeal to both institutional and retail (mum and dad) investors.

Funds raised by issuing urban infrastructure investment products would capitalise a special purpose statutory investment vehicle – the Urban Infrastructure Fund - that would then provide attractive seed finance to qualifying projects that meet criteria set by COAG in the form of local community infrastructure.

What is `Local Community Infrastructure'?

`Community infrastructure' refers to investment projects in metropolitan and regional communities across the country.

Some examples of local infrastructure are:

- transport – public and active travel transport systems, railway crossing pinch points;
- energy – low carbon precinct power and water capture;
- resilience – coastal management, levees, flood control, stormwater;
- community, cultural and recreational facilities;
- learning, health, aged care, seniors facilities;
- housing facilities – affordable housing projects; and
- protecting and enhancing biodiversity and ecosystem services – community waterways and grassland/woodlands.

The elements of the basic model are outlined in the following sub-sections:

1. credit-enhanced investment products – what do they look like?
2. eligible priority projects – what are the criteria?
3. issuing financial instruments – the role of Government and intermediaries;
4. project sponsors – who are they and what are their obligations?
5. complementary finance instruments – how can infrastructure project finance be further leveraged?
6. Urban Infrastructure Fund – how would it be run and governed?
7. supporting processes – what else needs to be considered?

Some Frequently Asked Questions are also provided at the end of this section.

The funding mechanism and institutions proposed in this section are intended to complement both traditional sources of infrastructure finance and other innovative capital raising techniques.

1. Credit-enhanced infrastructure investment products – what do they look like?

Community Infrastructure Investment Products *...enhance returns and manage risks*	The goal is to develop long-dated investment products that deliver guaranteed total returns that are more attractive than standard government bond rates. This will require credit-enhancement as generic infrastructure-related returns are not high enough to appeal to investors. Two techniques are proposed: • a tax rebate of 10% for investors purchasing bonds that finance eligible projects within the Urban Infrastructure Fund pool • a capped government guarantee.

2. Eligible priority projects – what are the criteria?

Eligible Projects *...to be recommended by Infrastructure Australia*	The broadening of Infrastructure Australia's remit to identify projects that qualify for credit enhancement is proposed. In addition to its current priority-setting role, Infrastructure Australia would identify community–level infrastructure projects that meet criteria, including: • COAG cities benchmarks • positive cost-benefit (including non-economic) criteria across city networks • capacity to generate sustainable cash flows or cross financing from reliable sources • capacity to provide/attract co-funding using complementary financial instruments • the quality and track record of project sponsors • demonstration of partnerships with local governments, state and territory governments, private sector and NGOs to deliver outcomes • inclusion of a set of indicators and/or targets and a robust, independent method of measurement to ensure that criteria are being met and desired outcomes achieved • there is a strategic basis for the project • there is demonstrated commitment to quality urban design, good architecture and sustainability. Guided by COAG, Infrastructure Australia would establish investment categories to ensure an optimum spread of project priorities – for instance, regional towns, outer metro growth areas, rejuvenation corridors, new master planned communities, low carbon/eco efficient networks, coastal adaptation zones. Infrastructure Australia would also regularly publish a list of projects that indicate a long-term investment pipeline. This would demonstrate deal flow opportunities to capital markets players.

3. Issuing financial instruments – the role of government and intermediaries

Australian Office of Financial Management (AOFM) *...to manage capital raising*	AOFM would manage bond issues on behalf of the Urban Infrastructure Fund. AOFM would liaise with financial market intermediaries. Funds secured by capital raisings would be transferred to an Urban Infrastructure Fund. AOFM would also pool and securitise bundles of prospective infrastructure asset income streams to ensure they are of sufficient scale to attract institutional investors.

4. Project sponsors – who are they and what are their obligations?

Project Sponsors *...would submit eligible projects for funding*	Project sponsors, such as local governments, statutory authorities, or regional development corporations would: • make applications for funds based on eligibility criteria • develop joint ventures with other government, private sector and NGO partners • agree to contractual delivery conditions • secure complementary funding streams that utilise approved financing pathways • provide plans for managing counterparty risk • provide evidence of capacity to manage the operating (post construction) phase of an asset.

5. Complementary financial instruments – how can infrastructure funds be further boosted?

Complementary Financing

...to diversify lines of credit and reduce reliance on the Urban Infrastructure Fund's capital

Project sponsors would complement Urban Infrastructure Fund seed capital with finance from partners and sources that may include:

Traditional Government

- Recurrent expenditure
- Other government infrastructure funds
- Other government incentives – NRAS etc.

Non-Traditional Government

- Local asset-backed vehicles (LABV)/joint project development (JPD) techniques
- Tax increment financing/growth area bonds
- Sale/lease back
- PPPs

Market Instruments

- Bank finance
- Covered bonds
- Corporate bonds
- Mezzanine/hybrid finance
- Other asset backed securities
- Other securitised/REIT index-linked structures

6. Urban Infrastructure Fund – what would it do?

Establish a Dedicated Fund

...with governance arrangements that boost investor confidence

The primary task of the Urban Infrastructure Fund is to:

- manage disbursements of funds to sponsors of eligible (Infrastructure Australia-approved) projects, backed by strict performance contracts
- ensure performance against contracts.

The Urban Infrastructure Fund would also help match-make syndicates of project sponsors and facilitate financial package design.

In addition, the Urban Infrastructure Fund would:

- work closely with ratings agencies to develop credible early warning systems
- facilitate investment tranche design.

The Urban Infrastructure Fund would seek to support investor confidence through:

- transparent regulatory controls and reporting that reduce the potential for default
- providing information on deal flow
- standardising financial information requirements (with AOFM) – simplified PDS etc.
- developing a national database of projects (commenced and completed) with an assessment of the community dividends expected and delivered.

7. Supporting processes – what else needs to be considered?

What else...	Fostering an informed market... • promote a reputable index of Urban Infrastructure Fund products • foster an investible index Reduce the Federal Government's cost of providing guaranteed support... Utilise a suite of quarantining measures to classify government guarantees as a contingent liability – and, thereby, not incorporated on the Government's balance sheet, such as: • time-limited guarantees • 'burning off' guarantees upon pre-agreed milestones • guarantees restricted to agreed metrics (with the balance of risks hedged) • guarantees linked to specified credit tranches (supplemented by complementary non-guaranteed financial products, such as mezzanine or equity components). Capital Management Explore opportunities to effectively transfer capital deductions (depreciation etc.) to the long-term owners of infrastructure.

Frequently Asked Questions

Q: *Infrastructure Bonds – What are they?*

A: Infrastructure bonds are a financial product designed to increase private sector investment in critical infrastructure projects.

These bonds attract private investment through a tax rebate on a proportion of the interest earned from an investment.

This credit-enhancement increases the return on projects so they compete more effectively with alternate investment products.

The tax rebate represents tax revenue foregone rather than an increase in government debt.

The infrastructure bonds introduced in the mid 1990s reduced borrowing costs by 40% compared to conventional borrowing expenses. They were poorly designed and subsequently scrapped; however, the concept remains sound.

A proposal previously considered by the Coalition estimated that an incentive (tax foregone) of $150 million would leverage $20 billion of new infrastructure investment.

Q: *Asset Backed Securities – What are they?*

A: Asset Backed Securities (ABS) are an investment product that combines the expected income streams of underlying assets – typically mortgages, credit card debt, car loans – into a pool that is then securitised – that is, offered to investors as bonds or notes.

The value of an ABS lies in the quality of the underlying assets in the pool and the prospect of consistently tapping into the stream of revenue generated by such assets over the long-term.

Q: *Is there a model for governing the proposed Urban Infrastructure Fund?*

A: The proposed entity is a financing authority and requires individuals skilled in governing finance and investment entities.

The guardians of the Future Fund provide one model.

The board should also include individuals experienced in all aspects of infrastructure procurement.

Q: *Are there any models for the Urban Infrastructure Fund?*

A: The financing instruments proposed in this paper are used in dozens of cities around the world.

Two examples of entities that specialise in local government finance are:

- Municipal Finance Authority of British Columbia
- New Zealand Local Government Financing Agency.

The United States operates a widespread `muni' (municipal) bond market.

Nevertheless, the concept proposed in this paper relies on the pooling of income streams from entities with marginal (but long-term) cash flows. The concept also utilises Australia's unique superannuation system – which is why a special purpose entity is proposed.

Q: *What is the Urban Infrastructure Fund likely to finance?*

A: Firstly, the Urban Infrastructure Fund will provide seed finance to quality projects. It is expected that project sponsors will also secure complementary capital.

The elements of the qualifying criteria are outlined in chapter five.

In addition, finance would focus solely on development and redevelopment capital, not meeting operational costs.

Q: *What should the scope of the Fund cover?*

A: The scope of the Urban Infrastructure Fund could cover both Nation Building Projects as well as Community Infrastructure.

Nation Building Projects - These are large-scale projects with capital construction costs greater than $100 million, such as transport projects. These projects will be assessed by Infrastructure Australia and aimed at driving productivity and equipping Australia for a low-carbon future. The criteria for this scale of infrastructure should build on Infrastructure Australia's existing categories and Nation Building 2's themes. However it should not be restrictive and there should be no exclusion of any type of infrastructure as long as it meets productivity, liveability and sustainability goals.

Community Infrastructure Projects – will include projects such as community, cultural and recreation facilities, learning, health, aged care and seniors facilities.