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To whom it may concern

On behalf of the Lord Mayors of Australia's capital cities I welcome the opportunity to provide a submission to the Productivity Commission in response to the Commission's draft report into public infrastructure released on 13 March 2014.

This submission builds on the Council of Capital City Lord Mayors' (CCCLM) earlier submission to the Commission's inquiry into ways to encourage private financing and funding for major infrastructure projects, including issues relating to the high cost and the long lead times associated with these projects.

High level observations

An Ernst and Young (EY) report commissioned by the CCCLM in relation to financing options for city infrastructure recommends that the most cost effective means for capital city councils would be to access loans through State Treasury Corporations. This option is not currently available to the City of Melbourne and Sydney. Furthermore, without Federal Government tax concessions, public bonds remain less competitive than capital city councils accessing conventional bank loans.

The CCCLM welcomes the recent in-principle agreement between the Federal and State and Territory Treasurers to enter into partnerships to undertake asset recycling to increase Australia's infrastructure stock. The Federal Government's incentive payment of 15 percent of the assessed value of the asset is a welcome step to encourage the unlocking of funds from existing assets to invest in building new public infrastructure.[1]

A report jointly undertaken between Urbis and the CCCLM identifies that "smart growth" reduces the cost of infrastructure by minimising the need to spend on new infrastructure. Smart growth is about making the best use of existing infrastructure through integrated land use and infrastructure planning. Case studies of smart growth in Australia's capital cities demonstrate that focusing public and private investment in areas where advantage can be made of existing infrastructure creates economic value by reducing costs of infrastructure and service delivery, providing redevelopment and reuse opportunities and stimulating business activity and job creation in these locations. Some preliminary financial analysis of this is provided and indicates that well targeted investment in public infrastructure, especially augmenting existing services, in urban centres can unlock many millions (if not billions) in private sector

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[1] Treasurer Hockey Media Release, 28 March 2014

investment in housing, office, and retail spaces, generating billions in economic activity, and avoid costly delivery of new infrastructure.

As advised in our earlier submission, collectively the the capital city councils administered around $35 billion in assets and injected over $4.7 billion into the Australian economy in 2012/13.[2] The economic and population load faced by Australia's cities is set to grow into the future, with our capital cities forecast to grow by 10 million people more by 2056.[3] Managing this growth and maximising opportunities will require cooperation and partnerships between Australian governments. In particular, governments will need to work together to plan and fund major infrastructure.

Responses to specific questions

Provision, funding and financing

Various public and private financing models may have a role to play

5.1 The Commission seeks feedback on the availability of bond finance for public infrastructure projects in Australia

- *To what extent are there impediments to the development of the Australian bond market to support investment in infrastructure?*
- *To what extent are there barriers to Australian infrastructure firms accessing international bond markets?*
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In August 2013 the CCCLM released research authored by EY examining the infrastructure needs and funding capacity of Australia's capital cities councils (note – Darwin and Canberra were not included in this research). Entitled *Infrastructure Financing Solutions for Australia's capital cities* the research examined the borrowing needs of capital cities and potential financing mechanisms including bank loans, public and retail bonds and borrowings through State Treasury Corporations.

The EY report found that most cost effective means for capital city councils to finance public infrastructure was through State Treasury Corporations loans (and likely to remain so in the short and medium term).[4] These loans are accessible by the cities of Brisbane, Perth and Hobart, with Adelaide able to access loans through the Local Government Financing Authority (LGFA) which borrows from the State Government.[5] Significantly, the City of Sydney and City of Melbourne are unable to access State Treasury Corporation loans, a situation with the CCCLM argues should be remedied.

Significantly, in regards to the use of bonds to finance public infrastructure, EY found:

- while public Australian bonds are a key source of funding for the Commonwealth, State and Territory governments, councils in Australia have not raised debt in this market (in essence because it is not the most cost effective means of financing local council scale projects, with the exception of the Brisbane City Council which delivers projects of scale atypical of most local councils).[6]

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[2] Combined Capital City operating and capital budgets 2012/13

[3] ABS *Labour Force Survey (Cat:8291.0.55.001)*, June 2012 – Excludes ACT and NT due to unavailability of city data

[4] Infrastructure financing solutions for Australia's capital cities, EY, July 2013, p29

[5] Ibid, p31

[6] Ibid, pp20, 29

- local councils could, but don't, issue unregistered debt securities (negotiated between an issuer and a limited number of investors in a private and unregistered transaction), and EY suggests this is not an appropriate mechanism for councils [7]
- local councils in Australia have not issued retail bonds and this mechanism is not appropriate for councils.[8]

According to this research public bonds are simply not the lowest cost financing method available for local council scale projects, with significant upfront and ongoing costs of arrangement and insurance diminishing the cost effectiveness of issuing bonds for small issuances (i.e. individual projects). EY found conventional bank debt to be a more cost effective financing means for local councils than public bonds.[9]

EY did not model how public bonds could fit local council needs, but suggested that the following arrangements would be required to improve the cost effectiveness of this mechanism:

- councils pool their borrowing needs (to achieve project scale)
- Federal Government tax concessions for lenders to drive down the borrowing cost for councils

EY also noted that structural reform of local government could impact the financial positions of capital cities, with amalgamations likely to impact their ability to raise revenue and service debt, if revenue strong capital cities were merged with councils in weaker financial positions.[10]

A complete copy of EY's report is available at: www.lordmayors.org and enclosed is a high level summary of this research.

Better institutional and governance arrangements are crucial

7.1 The Commission's current inclination is that the package of measures proposed in this report would be sufficient to constitute a 'pipeline' that would assist purchasers and tenderers in forward planning and to minimise costs. The Commission seeks views on the appropriate organisational framework to collect and disseminate information about a pipeline of projects and the extent to which private organisations should provide information about their plans to build significant infrastructure.

Private organisations as well as all levels of government should provide information about plans in line with a specific place-based strategic plan. Collaboration is needed to ensure effective strategic planning so that infrastructure is planned and delivered at the appropriate time.

7.2 The Commission seeks further information from participants on the costs and benefits of land corridor and site preservation strategies. In particular, it seeks evidence on the effectiveness of current jurisdictional strategies and the merits of a national regime. It also seeks views on the optimal ways in which corridors and sites can be used prior to infrastructure developments.

Last month the CCCLM released research it partnered with Urbis to produce *Smart Growth: Unlocking Smart Growth in Australia's Capital Cities* which examines examples of high quality development in Australia and internationally and identifies pathways to deliver more "smart growth" in Australian cities.

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[7] Ibid, pp21, 30
[8] Ibid, pp 21, 30
[9] Ibid, p29
[10] Ibid, p10

In regards to infrastructure, this research suggested that government should adopt a precinct-based approach for new investment in cities and prepare metropolitan plans with a single investment framework integrating land-use and development, transport and infrastructure investment.[11]

At its core, smart growth involves planning our cities so that they are accessible places to live and work; distributing land uses and activities, and designing cities and communities in ways that minimise travel time and cost.[12] The research highlights that smart growth achieves an equitable distribution of the costs and benefits of development together with lower investment costs through efficient use of existing infrastructure to support population growth. Smart growth seeks to shift the focus on new buildings and infrastructure and look at ways of better using existing assets:

- using models of infrastructure and financing that ensure the maintenance of existing assets
- supporting infrastructure projects with complementary investment in new social infrastructure and land uses
- encouraging creative infrastructure solutions, including renewable generation options such as co-generation and tri-generation[13]

Significantly, strategic infrastructure investment is key to unlocking smart growth opportunities. Urbis highlighted the critical role that well targeted investment in public infrastructure has performed in unlocking billions of dollars of private sector investment in Australia's cities, including:

- Brisbane City Council's Newstead – Teneriffe Area – Federal Government invested $22M through the *Building Better Cites Program* for sewerage works to unlock intense development delivering over 6,500 new homes [14]
- Canberra's City West – ACT Government invested $18M to improve public spaces including pedestrian lighting, street furniture, paving and landscaping, unlocking approximately $1B in private sector investment [15]
- Melbourne City Council's Melbourne City, Postcode 3000 – VIC Government invested in an underground rail loop and three new underground stations to improve connections throughout the city, coupled with the City of Melbourne embarking on pedestrianising the CBD, enabling 30,000 residential dwellings to be built in the CBD in just over 15 years.[16]
- City of Sydney's Harold Park – taking advantage of existing bus networks and utilising the underutilized Jubilee light rail station, the City of Sydney aims to unlock $1.1B in private sector investment [17]
- SA Government's Bowden Urban Village in Adelaide – SA Government invested over $246M to unlock up to $1B in total investment [18]
- WA Government's Subi- Centro – WA Government invested $200M in rail projects (including sinking the railway line and constructing a new railway station), enabling better land connections, unlocking $960M in private sector activity [19]

A complete copy of Urbis' report is available at: www.lordmayors.org and enclosed is a high level summary of this research.

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[11] Smart Growth: Unlocking Smart Growth in Australia's Capital Cities, Urbis, March 2014, p6
[12] Ibid, p22
[13] Ibid, 23
[14] Ibid, p101-105, p32
[15] Ibid, p111-114, 38
[16] Ibid, p95-100
[17] Ibid, pp115-119, 34
[18] Ibid, pp90-94
[19] Ibid, pp106-110, 37

In regards to corridor and site preservation strategies, this is important nationally and particularly important in inner-city renewal areas, such as Green Square in the City of Sydney. Investment in corridor preservation is not a true infrastructure cost, but a reservation of land can minimise infrastructure costs when development warrants planned infrastructure.

The City of Sydney has found that purchasing land corridors at an earlier stage, prior to other developments taking place, results in dramatically reduced brownland site acquisition costs. If for any reason the construction of infrastructure does not proceed, the land corridor can be–on-sold to the private sector (or retained by government) for other uses. If on-sold, the original land cost could be repaid and any value capture retained to finance alternate infrastructure or to take advantage of newer more efficient technologies.

The process itself presupposes the development of place-based Land-use and Economic Strategic Plans, which in turn require collaboration between levels of government (responsible for different forms of infrastructure as well as the private sector) and a concurrence on the magnitude and timing of growth paths of residents and employment. Whilst logically this would suggest a State-Local Corridor "bank" institution, in the interests of transparency and co-ordination with other significant national infrastructure, such a funding facility is best located at a national level.

Reducing costs

Planning and tendering arrangements can be significantly improved

11.1 The Commission seeks evidence on the skills of public sector clients to manage contracts for major infrastructure projects. Is there evidence that a relative lack of skills has led to systematic cost overruns during the delivery phase? How does this compare to the performance of private sector clients?

Both public and private sector project managers need the highest quality skills. This can only come from education and proper vetted certification of courses available as well as practical experience.

Whilst the private sector may be driven by profits, the public sector can be driven by the requirements to achieve goals and targets from an over-arching Strategic Plan, with equal accountability for performance.

Examples can only be individually-based and not generic. Moreover, it is not merely a matter of the scale of project management experience. A larger or more expensive project is not necessarily any more complex than a smaller-scale project, which can often be extremely complex in terms of risk management, stakeholder engagement, and quality control. Arguably, particularly at a local level, public sector employees can have access to and awareness of particular local factors that can dramatically affect project outcome.

In its report for the CCCLM, EY observed that the capital cities are generally relatively sophisticated and can attract high quality staff, due to their location, status, budget and perceived career opportunities.[20] Improvements in asset management techniques are delivering councils better whole of life costs associated with infrastructure.

[20] Infrastructure financing solutions for Australia's capital cities, EY, July 2013, p10

Better data collection and some reviews are required

8.3 The Commission seeks further and better evidence on construction cost differentials for major infrastructure projects, both within Australia and between Australia and comparable countries.

There will be spatial variation of construction costs within Australia because of the higher site acquisition costs in brownfield areas, particularly in the inner part of the major cities. Any assessment of infrastructure needs to be more than just cost-based but also relate to the benefits to be derived – with those benefits likely to be greater to more people in areas of highest density.

As indicated in our previous submission, land costs, labour costs, physical capital, and cost of financing vary significantly across different projects and are individual project sensitive. Large scale infrastructure or major projects attract a significant delivery overhead in relation to stakeholder engagement, project controls and required government authorities' consents, approvals, and review.

The CCLCM would be delighted to discuss our submission with you in more detail. Please contact me on 02 6285 1584 or [redacted] if you would like further details.

Yours sincerely

[redacted]

Cheryl Thomas
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Council of Capital City Lord Mayors

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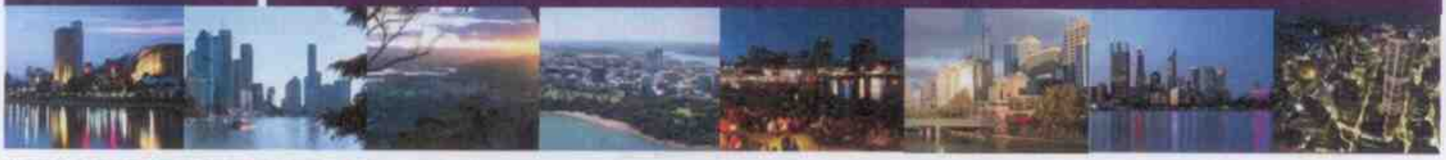

INNOVATIVE INFRASTRUCTURE FINANCING

Australian Governments are facing a growing demand for public infrastructure projects coupled with a diminishing capacity to pay for this infrastructure through core revenues. New research has been undertaken to explore innovative financing mechanisms available to help build the infrastructure our nation needs.

Local government delivers a range of infrastructure, including local roads, bridges, footpaths, water and sewerage (in some states), drainage, waste disposal and public buildings (libraries, community facilities etc). Providing and maintaining infrastructure is one of the most important responsibilities faced by Australian capital city councils, but it also presents one of their largest challenges.

OVERVIEW

Research conducted by EY on behalf of the CCCLM concludes that the extent of the infrastructure task in Australian capital cities is significant, and not getting any smaller, evidenced by indicators such as high demand for assets, maintenance backlogs and rising renewal costs. In light of this, capital cities are investigating their funding and financing capacity and the way to apply capital to addressing the challenge.

CAPITAL CITIES AND DEBT FINANCE

While debt finance in the form of conventional bank loans (or in some jurisdictions, Treasury Corporation loans) is readily available to councils in Australia, the local government sector has not been able to use its strong credit fundamentals to leverage sources of debt that attract the most favourable pricing, nor has it been able to tap into or create an interface with the institutional investment market.

Compared with other types of local government, capital city councils are unique in their capacity to leverage own-source revenues. Capital cities are also unique in respect to the nature and size of projects undertaken.

But debt plays a small role in the balance sheet of most capital cities. Some have no debt at all, and the majority have a debt service coverage ratio (representing the ability to repay debt) well above the national average for all local government in Australia.

There is therefore an opportunity for capital city councils to use innovative funding solutions to deliver infrastructure projects.

In the context of sound financial management and project planning, the key benefits of optimising the role of debt within the capital structure are that it can:

- enable councils to deliver new infrastructure when it is required and earlier than they otherwise would have been able
- enable the funding and development of 'user pays' or other income-generating infrastructure such as toll roads
- allow the smoothing of the payments for new investment over time
- prevent the need to divert funds from internally-generated renewal and maintenance budgets to capital expenditure
- enable councils to invest in the renewal and lifecycle costs of existing infrastructure, which are time-sensitive and if not delivered can increase the whole-of-life cost of an asset
- allow the cost of infrastructure to be shared with future generations who will enjoy the benefit of the asset
- open the door to new sources of investment, for example from institutional finance providers, which bring additional rigour and discipline.

OPTIMISING THE ROLE OF DEBT

Australia's capital city councils are very well placed to move towards an optimal debt load supported by a range of sources. The key findings of the EY research are as follows:

- State Government Treasury Corporation loans are likely to remain the cheapest form of borrowing available in the short and medium term.
- For those councils that do not have access to State Government Treasury Corporation loans, conventional bank debt is likely to provide the most flexible and cost-effective form of debt finance for small and medium borrowing requirements.
- For those councils with larger borrowing requirements, significant savings might be achieved through issuing a public bond into the Australian market. Although bond issuance involves an element of cost and complexity, the relative saving for a large issue when compared with conventional bank debt can be material over the term of the instrument.
- Councils would be able to achieve a more favourable outcome from alternative borrowing solutions if they were to enter into collective arrangements with other councils, and give the market the opportunity to provide a lower cost of borrowing based upon the combined credit credentials and economies of scale associated with bundling.
- Any tax concessional arrangements for lenders in the future could drive down costs for borrowing councils and drive a more favourable outcome from alternative borrowing solutions that qualify for the concession.
- Any future borrowing activity would need to take regard of the legislative constraints that are placed on local government by state governments.
- US public bonds, US private placements, AUD private placements or AUD retail bond issuances are not considered suitable borrowing solutions for Australia's capital city councils at the current time.

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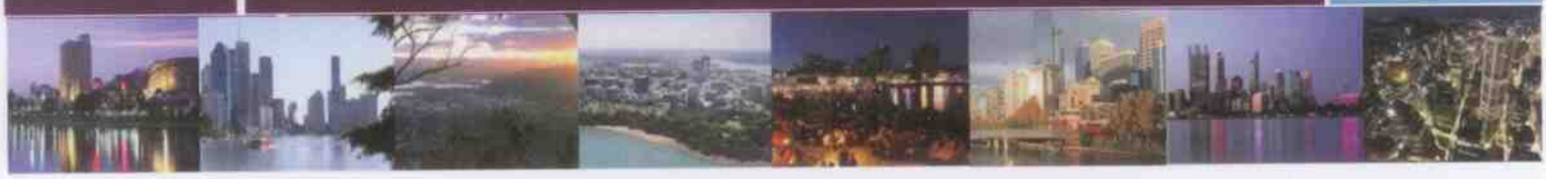

UNLOCKING SMART GROWTH IN AUSTRALIA'S CAPITAL CITIES

Federal leadership and investment is key to securing the wellbeing of urban communities and maximising national prosperity.

The investment decisions of government have a profound impact on the productivity and efficiency of cities. Traditional approaches to managing our cities are not sufficient to meet productivity, health and liveability challenges facing our urban communities.

New research by Urbis is examining how Australians would benefit from living and working in well planned cities. To be released in coming months, the research investigates 'Smart Growth', and the role of cities in improving community wellbeing and reducing fiscal pressure on government (local, state and Federal). International and Australian examples of 'Smart Growth' are being examined to identify tangible pathways to deliver more 'Smart Growth' more often in more Australian cities.

OVERVIEW

The Council of Capital City Lord Mayors (CCCLM) is partnering with Urbis to examine the benefits of 'Smart Growth' and identify pathways to achieve 'Smart Growth' in Australia's cities.

Australia's cities are growing in population and size. Nearly 1.3 million people moved to an Australian capital city in the 5 years to 2011 (79% of Australia's total population growth). Accommodating this growth is creating challenges:

- more expensive to build, operate and maintain
- growing gap between population growth and housing supply
- poor accessibility to jobs
- increase in 'lifestyle' diseases such as obesity and diabetes
- outward growth generating demand for new infrastructure and services

Managing the growth of Australia's capital cities is becoming increasingly complex and costly. The cost of adding a new dwelling, with supporting infrastructure, to new suburbs at the edge of the city is nearly twice as expensive as building a dwelling in established parts of a city.

WHAT IS SMART GROWTH?

Smart Growth is an integrated approach to planning and developing cities based on 8 principles:

1. Highly connected places
2. Places that are easy to move to and through
3. Using land wisely
4. Using infrastructure wisely
5. Creating resilient and adaptable neighbourhoods
6. Enabling healthy lifestyles and choice
7. Shared long-term vision
8. Aligning public and private interests

See **www.lordmayors.org** for more information

Smart Growth involves more than just good planning, it requires:

- Investing in renewal in existing suburbs
- Providing all transport options including walkable neighbourhoods
- Neighbourhoods offering choice through a mix of land uses and opportunities
- A precinct and place-based focus on investment and urban management
- Optimising the use of existing infrastructure
- 'On the ground' delivery and integration

Smart Growth is not a quick fix. It requires a long-term view and approach to implement.

WHY AUSTRALIAN CITIES NEED 'SMART GROWTH'

Smart Growth can deliver:

savings - building communities in existing neighbourhoods reducing the need for new infrastructure
economic growth - catalyst infrastructure helps stimulate private sector investment and development
productivity growth - linking people and jobs
healthier communities - encouraging walking and cycling

ROLE OF GOVERNMENT IN DELIVERING SMART GROWTH

Smart Growth in Australians cities is achievable using the following 7 steps:

1. **Increase the priority given to the importance of Australian cities** within National Policy and Federal investment processes
2. **Adopt a precinct-based approach for new investment in cities**
3. **Enhance Federal Government funding for cities** via a Smart Growth paradigm
4. **Invest in developing and using strong evidence based knowledge** about the costs and benefits of building Australia's cities and using that knowledge to improve the effectiveness and efficiency of infrastructure investment
5. **Locate new urban growth in the right places** to optimise infrastructure investment, productivity, sustainability and improved quality of life
6. **Make connectivity and accessibility a key component** for all new urban development
7. **Create a virtuous cycle of value capture and re-investment in cities**

THE BENEFITS OF SMART GROWTH

The adoption of Smart Growth in Australian cities would result in significant benefits.

Economic Benefits of Transport Choice	Locating people close to a wide variety of services within easy walking, cycling and public transport minimises road infrastructure spend and optimises existing and readily upgradeable capacity within existing transport systems
Enhanced Catalytic Investment	Public investments based on Smart Growth principles - in compact and efficient development forms - generate substantial private investment, with associated economic, environmental and quality of life benefits
Optimum Investment and Use of Infrastructure	By prioritising investment utilising existing over new infrastructure, Smart Growth is fiscally prudent and creates the opportunity for more sustainable development based on new land use opportunities in established areas
Sustained Viability of Local Business and Greater Productivity	Smart Growth connects workers, businesses and customers through a focus on transport choice and creating the conditions for larger, more proximate workforces, increased foot traffic and more efficient distribution networks
Compact, Walkable, Connected Communities	Compact, mixed use urban forms, excellent public transport accessibility and active travel opportunities create the essential foundation for a variety of types of vibrant, healthy and walkable communities to emerge
Increased Active Transport	Well-connected, compact and highly accessible mixed use communities enhance opportunities for active travel and reduce the reliance on the car
Healthy Lifestyles	Smart Growth enhances opportunities for physical activity and social interaction and promotes independence through making short trips to access daily needs by walking or cycling appealing, which in turn helps to prevent illness such as diabetes, obesity and mental illness