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AUSTRALIAN PROPERTY INSTITUTE (Inc)
WESTERN AUSTRALIAN DIVISION

SUBMISSION TO

Department of Planning
Western Australian Planning Commission

IN REGARD TO

Draft State Planning Policy 3.7
Planning for Bushfire Risk Management May 2014

Prepared for API (WA) by:

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Planning for Bushfire Risk Management
SPP 3.7 submission
Department of Planning
Locked Bag 2506
Perth WA 6001

By email: bushfire@planning.wa.gov.au

RE: PLANNING FOR BUSHFIRE RISK MANAGMENT SPP3.7 SUBMISSION FORM

API (WA) is pleased to provide this submission to the Department of Planning in regard to the *Draft State Planning Policy 3.7 - Planning for Bushfire Risk Management* May 2014 (SPP3.7).

The Australian Property Institute (API) was originally formed in 1926 as the Commonwealth Institute of Valuers. The Institute has undergone several name changes over the last century as the array of property professionals connected to the Institute expanded.

Today the API represents the interests of more than 8,600 property professionals throughout Australia. API members include residential, commercial and plant and machinery valuers, property advisers, property analysts, property fund and asset managers, property facility managers, property lawyers, and property researchers and academics.

The Institute plays an integral role in the property sector in this State and presents impartial commentary and professional development on all aspects of the Industry.

Executive Summary

The importance of the safety and protection of people, property and infrastructure from the impact of bushfires is clearly understood. However, it is important that any unintended consequences of a broad based instrument such as a state planning policy be taken into account.

The API believes that the proposed SPP3.7 will have a significant impact on land value, urban development, and broader land use planning.

Consideration must be given to a number of transitional challenges including potential permanent impacts that will be imposed on property as a result of implementation of the proposed SPP3.7. Our concern is that the draft policy does not appear to have addressed property valuation, mortgages or insurance issues.

Sections of this policy which act to apply bushfire controls, do not necessarily consider:

- implications for adjoining landholdings arising from vegetation within median strips, buffers, revegetated areas and public open space
- Impact on property value
- Effect on current property zoning and development approvals
- Financial institutions disposition to lend or refinance on properties
- The highly problematic nature of undertaking insurance replacement valuations
- Compensation matters for existing properties which will be negatively impacted

Some of these matters arise due to:

- The restrictions imposed on existing properties

- The ‘one size fits all’ approach of the proposed policy which fails to differentiate between the very different contexts of urban and peri-urban, or transitional, development.

Our reading of SPP 3.7 raises concerns that the broad impact on the market value of property and the ability to value, finance and insure properties has not been fully considered.

Scope of this submission

API will be making a separate submission to the guidelines. It should also be noted that these comments have been provided prior to the release of the bushfire-prone area mapping as well as the bushfire regulations. Future release of associated bushfire documentation, including the mapping and regulations, may alter the effect of this policy and, this submission.

While the membership of the Australian Property Institute (API) includes a wide cross-section of property professionals, the Institute is the professional home for the significant majority of licensed valuers in Western Australia and Australia. The API submission will focus on the perspective of property valuation.

Institute’s which more particularly represent the interests of developers and planners etc. will undoubtedly make submissions from the perspectives of the professionals represented by them and we will liaise with those bodies on matters which impact across these sectors.

The comments included in this submission are limited to the Draft State Planning Policy 3.7, with any references to the associated guidelines intended only to clarify the relevant sections of the SPP.

Property Valuation

Individual Property Rights

SPP3.7 and the Guidelines impose an entire new level of assessment criteria that override existing planning regulations and property rights. Those existing planning regulations and property rights (and the expectation that they will remain constant into the future) are the basis upon which property values are established.

By overriding existing planning regulations, the SPP3.7 and Guidelines will alter the existing development potential of affected properties and hence impact on individual property rights, which in turn have a detrimental impact on the market value of a property.

SPP3.7 has the potential to impact on individual property rights in the following ways:

- The uncertainty of the ability to develop a property to its current maximum potential as permitted under its existing zoning and planning regulations.
- The increased costs of construction.
- Assessment of insurance replacement costs for existing properties developed prior to SPP3.7.
- Finance industry uncertainty on the underlying market value of properties located within the State Bushfire–Prone Area Map

Assessing a Value on Property

Under the proposed Bushfire Risk Management Policy even the possibility of areas being classified as bushfire prone will have a detrimental impact on property values. With the significantly increased development standards to apply; the costs of initially developing (subdividing) the land will be significantly greater. In addition the construction costs of the residences to then be constructed will increase due to the higher levels of fire tolerance required.

Prospective purchasers of developed lots will expect to pay less as the cost of construction of a single residence will be higher. This will impact on the value of the development site as the gross realisation will be less and costs of development higher.

Given the uncertain requirements of both of the above, the level of subjectivity applied in endeavouring to assess the affected value of the properties in these locations will be significantly greater than normal and will be subject to significant disclaimer provisions.

The likely effect of this is that financial institutions will find this unacceptable; prompting a change to their lending policy in these areas - further impacting on property values as finance availability will detrimentally impact the number of potential purchasers and hence demand for these properties.

The result of this change will most likely increase over time as the full effects wash through the market and become more apparent. This will undoubtedly raise questions such as:

- Is compensation to be paid to affected land owners - as the value of these properties will be diminished?
- What is the period in which property owners will be able to claim this compensation?
- What is the time period for which compensation will be applicable (is this backdated)?

The following are hypothetical examples of value impacts of SPP3.7

EXAMPLE 1
Subdividable broadacre property into 10 lots Prior to SPP3.7

Gross Realisation							
	10	Lots @	$250,000	per Lot/Unit =			$2,500,000
Less	**Selling/Advertising Expenses**						
	Selling	2.00%	0f Gross Realisation			($50,000)	
	Advertising	0.20%	0f Gross Realisation			($5,000)	
	Legal	0.20%	0f Gross Realisation			($5,000)	
	Settlement	0.10%	0f Gross Realisation			($2,500)	($62,500)
Net Return/Realisation							$2,437,500
Less	**Profit and Risk Allowance**						
	Allow Say				10.00%		($221,591)
							$2,215,909
Less	**Development Costs**						
	Construction Costs					($1,000,000)	($1,000,000)
							$1,215,909
Less	**Interest on Development Costs**						
	(Half Construction and Selling Period)						
	3	Months @	8.00%	pa			($13,599)
Less							
	Rates and Taxes (Half Lots/Units)						
	10	Units/Lots @	$750	per Unit/Lot			($3,750)
							$1,198,561
Less	**Opportunity Cost on Land**						
	Total Project Period				6	Months	
	Interest Rate				5.00%	pa	($37,007)
LAND VALUE (Exclusive of Stamp Duty Allowance)							$1,161,553
Less							
	Stamp Duty on Purchase Price						$48,500
RESIDUAL LAND VALUE							$1,113,053

EXAMPLE 2

Subdividable broadacre property into 9 lots now in bushfire zone
(9 lots as development restrictions, buffer zones etc impact on optimum development costing at least one lot)
The value of each finished lot has been discounted by 20% to offset buyer resistance due to the increased cost of house construction. We have also estimated a 10% increase in development costs.

Gross Realisation							
	9	Lots @	$200,000	per Lot/Unit =			$1,800,000
Less	**Selling/Advertising Expenses**						
	Selling	2.00%	0f Gross Realisation			($36,000)	
	Advertising	0.20%	0f Gross Realisation			($3,600)	
	Legal	0.20%	0f Gross Realisation			($3,600)	
	Settlement	0.10%	0f Gross Realisation			($1,800)	($45,000)
Net Return/Realisation							$1,755,000
Less	**Profit and Risk Allowance**						
	Allow Say				10.00%		($159,545)
							$1,595,455
Less	**Development Costs**						
	Construction Costs					($990,000)	($990,000)
							$635,455
Less	**Interest on Development Costs**						
	(Half Construction and Selling Period)						
	3	Months @	8.00%	pa			($12,239)
							$623,216
Less	**Rates and Taxes (Half Lots/Units)**						
	9	Units/Lots @	$750	per Unit/Lot			($3,375)
							$619,841
Less	**Opportunity Cost on Land**						
	Total Project Period				6	Months	
	Interest Rate				5.00%	pa	($23,456)
LAND VALUE (Exclusive of Stamp Duty Allowance)							$596,385
Less	**Stamp Duty on Purchase Price**						$21,350
RESIDUAL LAND VALUE							$575,035

Value of property is generally considered to be an issue for the property owner – however the implementation of SPP3.7 would also impact what can be done with the security in that property – creating a multiplier effect. The issue is also for the mortgagee and the council's rateable value. That is to say that there will not only be an immediate effect on values – but a flow-on effect - a gradual unwinding of value and flow on to the finance industry

In the case of a house being destroyed - you may not be able to rebuild your home – so the property might be revalued at a significantly reduced land value only.

The Policy applies across the whole of the State – requiring valuation of all properties to take into account the possible impact from the policy.

Property Owner

The property owner often enters into the property transaction with a view on the ability and cost to develop or redevelop a property, based on an understanding of the current zoning. The proposed policy may affect the property owners' ability to undertake any or all of those options and result in a range of financial implications.

This will apply to both developed and undeveloped properties. SPP3.7 as it is currently proposed has the ability to override the zoning on a property and be the ultimate determining factor in the development potential for that property. This represents a significant risk to existing owners (and their financiers) given they purchased a property based on the development potential permitted under the current zoning. To reduce or restrict the development potential of a property (and/or cause a significant increase in construction costs) will result in a direct reduction in the market value of a property.

For developed properties, the risk lies in the ability to either replace (for example, in the event of a disaster) or redevelop a property. With an undeveloped property, SPP3.7 creates a risk in that it may reduce the current development potential from what is permitted under its current zoning. For example, a property that is capable of subdivision into a certain number of lots under its current zoning may be required to reduce the number of lots in order to meet the requirements of SPP3.7 and the Guidelines.

Given the potential impact on property values, strong consideration needs to be required on how such issues will be addressed prior to the implementation of SPP3.7

Involvement of Financial Institutions

Financial Institutions are often the first involved in property transactions and will then instruct a valuer. If the property is in a designated bushfire prone zone it is likely the bank will either impose tighter lending criteria on such property or potentially not consider the risk acceptable

Also, the unintended retrospective application of the Policy may prove adverse to the Market Value of properties with existing debt facilities. This may result in covenant breaches upon revaluation in the context of the Policy and the client will be placed into the bank workout units unless debt can be reduced or alternate/supplementary security provided.

The effect of this may not be fully comprehended until property transactions occur and could result in an expectation that valuers will be asked to create rather than interpret the market, which is an unacceptable situation within a normal functioning market and the question then being "what will become of these areas".

This may well lead to a requirement for the development of a State specific (WA) lending policy, which could well include properties falling within certain classifications under the Policy being deemed as unacceptable security.

Additionally, the requirement for borrowers to provide a bushfire hazard assessment and/or Bushfire Attack Level (BAL) assessment may form part of the abovementioned lending policy as a condition precedent to funding. From a commercial perspective, this would be another cost impost (additional to valuation fees, establishment fees etc.) on clients that are adverse to any further expense as part of the loan application process.

The possible for diminution in security property values would also have regulatory consequences, with APRA overview of lending institutions' valuation books ongoing.

Developers/buildings will likely not consider pricing up homes in these areas

From discussions with representatives of one of the largest building firms in Western Australia, concerns have been expressed about the difficulty in meeting BAL requirements. At present they have found that meeting requirements for the lower BAL ratings, i.e. BAL-12.5 and BAL-19, can be achieved through adaptations to existing standard designs. However, these adaptations are still increasing the cost of construction to anywhere from 5% to 10% above the standard cost of that home.

For higher BAL ratings however, adaptations to standard designs will not be possible and those affected properties will require site specific designs combined with the use of non-standard materials, which are likely to cause significant increases in construction costs, well above the 10% currently being experienced for a BAL-19 rating. At present this builder has avoided offering their services for properties with ratings above BAL-19, due to the complexity of the designs and the unaffordability of those homes.

If mainstream builders are not willing to operate in this sector of the market the economies of scale they bring the home construction market (leaving this to the domain of specialist builders) will limit the choice for owners and ultimately increasing building costs further.

Given the current affordability crisis within the Perth housing market, serious consideration needs to be given to the practical implications of SPP3.7. To add up to 10% above the cost of standard homes in the lower BAL rated areas and significantly more to homes with a higher BAL rating, will further exacerbate the affordability crisis and also cause additional financial hardship to existing owners of undeveloped sites.

<u>Compensation</u>

As referred to above, potential claims for compensation will arise in circumstances where the maximum development potential of a property as permitted under its current zoning is reduced by the application of the of SPP3.7. The current premise upon which the property market operates, that is, assessing the rights afforded to a property based on its current zoning will not always be applicable and this has serious consequences for the property market in pricing and valuing affected property.

Although it is an unintended consequence of SPP3.7, it is a very real prospect and to not otherwise consider the issue of compensation in such circumstances would create a great deal of financial hardship for affected property owners.

Again this will apply to both developed and undeveloped properties and has the potential to create great uncertainty within the communities located in the affected areas.

<u>Conclusion</u>

The Australian Property Institute (WA Division) submits the above as its initial commentary on the *Draft State Planning Policy 3.7 – Bushfire Risk Management*.

We recognise that significant elements which will underpin the operation of the proposed policy are not available at this time. These include definition of the areas which are to be identified as being bushfire prone and the proposed State Bushfire-Prone Area Map; the accreditation scheme for fire consultants in Western Australia; training framework for the decision-makers (to assist them to understand and interpret the expert advice provided); resourcing of relevant agencies and approval authorities to administer additional responsibilities to ensure that procedural delays are minimised.

Please feel free to contact us if further clarification of any elements of this submission is required.

Yours sincerely

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