

**Incentives and disincentives:
The potential of property taxes to support
public policy objectives**

Phil Day



Urban Policy Program

**Issues Paper 4
January 2005**

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Griffith University
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www.griffith.edu.au/centre/upp

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THE AUTHOR OF THIS ISSUES PAPER

Dr Phil Day (retired) is a planning consultant, academic and public servant and resides in Toowong, Brisbane.

Editorial assistance was provided by Nick Buchanan of the Urban Policy Program.

Contents

Introduction	5
The concept of betterment and betterment levies	5
Legislative history of betterment levies	6
The Sydney betterment levy	7
The ACT betterment levy	9
The conditions precedent	10
Limitations	11
Surrogate betterment levies	13
Reviewing the present situation	14
The Greenhouse Factor	15
Compensation law and philosophy	16
Conclusion	19
References	21

Introduction

Sumptuary taxes like those on alcohol and tobacco illustrate how fiscal measures can be used to achieve public policy objectives. Yet the fiscal measures that are the main source of public revenue in Australia, namely taxes on income, capital and labour, do not reflect any policy objective other than revenue raising; indeed, if producing socially desirable goods and services is a public objective, they have a disincentive impact. On the other hand, charges levied on the use or possession of land or other community resources can impact directly on policy outcomes. While such charges are currently not a major source of public revenue, their potential utility as policy instruments (and a significant revenue source) deserves to be explored.

The concept of betterment and betterment levies

A starting point is the concept of publicly initiated community betterment and the means by which public revenue can be raised to recoup the cost of it.

Betterment is an age-old concept. It can be defined as benefit or advantage conferred by a public authority on identifiable beneficiaries – its converse, ‘worsenment’ or ‘injurious affection’ is loss or disadvantage. Betterment levies are a means of recouping betterment. A betterment levy is a charge levied upon the beneficiaries to recover for the public authority/community some or all of the value of the benefit. If it is not recovered, the benefit or betterment is an unearned windfall increment in value conferred upon the private beneficiaries.

Recorded examples of betterment levies in the United Kingdom date back at least to the Middle Ages. An early example was the taxing of property owners who benefited from sea defence works; and later in 1662 charges were levied on the beneficiaries of street widening in London and upon beneficiaries of re-building after the Great Fire in 1667.

The older notion of betterment related to public works. In modern times betterment levies have become associated with the theory and practice of controlling land use through town and country planning. A particular focus has been on the consequences of town planning decisions (notably ‘rezoning’ decisions), which permit more intensive land use.

The older notion of benefit conferred by public infrastructure survives, however, for example in the case of pedestrian malls constructed by public authorities and financed in part by special local government rates levied upon the benefited properties. One distinction is worth keeping in mind. There is no theoretical limit to the quantum or duration of a special rate levied by a local government council, whereas, if betterment levies are adopted in the course of implementing town planning, they are normally a once-off levy imposed following a publicly authorised change of permitted land use which benefits the landowner.

Town planning theory has always recognised the logic of capturing betterment and compensating worsenment. Before reviewing the evolution of betterment in practice, however, the Australian context warrants some brief explanation. In pre-federation Australia,

capturing the 'unearned increment' in land values was the focus of many writers and advocates of land and tax reform in the latter half of the 19th century, especially after the visit of American socio-economic philosopher and tax reformer Henry George in 1890, and the Victorian land scandals of the 1880s. Indeed, efforts to prevent land speculation date from the earliest decades of settlement. And the notion of self-funding the infrastructure of the envisaged federal capital from land value increments led to the adoption of leasehold tenure for the proposed federal capital territory.

Legislative history of betterment levies

In England the principle that had been applied to certain localised improvement areas was revived in the *Housing (Town Planning) Act* of 1905, and further developed in the *Town and Country Planning Act* of 1932. These Acts allowed a local authority to claim 50 percent and 75 percent, respectively, of the amount by which the value of property was increased through the operation of a planning scheme. The 1932 English Act was the inspiration for post-war planning legislation in Australia, and similar betterment provisions were inserted in most of the early State planning acts. Like their English progenitor, however, the betterment provisions in the State acts were virtually a dead letter. Nevertheless in a landmark compensation case in NSW in 1954 (*Bingham v Cumberland County Council*), the NSW Land and Valuation Court held that compensation was offset by betterment accruing to other land of the claimant.

Thus the decision clearly acknowledged the concept of betterment conferred on landholders by public sector actions, and accordingly it supports the proposition that betterment is available to be captured (independently of worsenment and possible compensation).

Meanwhile probably the high-water mark in the evolution of betterment philosophy was the 1942 report of the Uthwatt Committee (the Expert Committee on Compensation and Betterment), one of the remarkable reports prepared in wartime England in anticipation of post-war reconstruction. The Uthwatt Committee adopted a comprehensive definition embracing any increase in the value of land arising from central or local government action, whether positively by way of the execution of public works of improvement, or negatively by way of the imposition of restrictions on other land. The Committee was disposed to include the enhancement of property values arising from general community influences such as the natural growth of population, whereas historically, increasing property values attributable to incremental growth have been subject to annual property rates levied by local government councils (on either the value of land or of land together with the improvements on it).

In post-war Britain, the 1947 *Town and Country Planning Act* that embodied the Uthwatt Committee's recommendations was a dramatic attempt to solve the problem of capturing betterment. In essence it reserved all (existing and future) development rights to the Crown and allocated a £300 million sterling sum to meet compensation claims for this loss of development. Thereafter it was envisaged that intending developers would buy back development rights by way of a development charge. Simple in principle, the scheme was rendered complex in practice by numerous savings, exceptions and modifications; land owners tended to withdraw from the market; and the inflationary impact of the proposed

£300 million payout caused apprehension. Successive Conservative governments repealed the 1947 Act and substituted for it a series of less memorable acts in 1953, 1954, 1959 and 1961. In 1967 the Labour government introduced the *Land Commission Act* which reintroduced a direct betterment levy, initially fixed at 40 percent, on the net development value of land used for development. The Commission and the levy were abolished by a Conservative government in 1971. Subsequent Labour and Conservative thinking has shifted away from betterment and tended to polarise around the upper and lower limits of public responsibility for land acquisition and development. The “elusive betterment”, as one English writer put it (Roberts, 1977), has remained uncaptured.

In 1976 the principle of capturing betterment was strongly re-affirmed in the ‘Vancouver Plan for Action’, the recommendations of the United Nations (Habitat) Conference for National Action on Human Settlements, which Australia endorsed. The preamble to the recommendations on land emphasised its special quality:

Land, because of its unique nature and the crucial role it plays in human settlements, cannot be treated as an ordinary asset controlled by individuals and subject to the pressures and inefficiencies of the market (United Nations, 1976, n.p).

The preface to an identification of specific ways and means declared:

The unearned increment resulting from the rise in land values resulting from change in use of land, from public investment or decision, or due to the general growth of the community must be subject to appropriate recapture by public bodies (the community), unless the situation calls for other additional measures such as new patterns of ownership or the general acquisition of land by public bodies (United Nations, 1976, n.p).

The reference to the wider concept of capturing the unearned increment resulting from the general growth of the community is interesting. So, too, was a sensible acknowledgement that public ownership of land “cannot be an end in itself” but:

should be used, whenever appropriate, to... implement urban and rural land reform processes, and supply serviced land at price levels which can secure socially accepted patterns of development (United Nations, 1976, n.p).

Thus the framers of the Vancouver Plan did not see land nationalisation as a cure-all solution.

The Sydney betterment levy

In Australia in 1967, the report of the NSW Royal Commission of Inquiry into Rating, Valuation and Local Government Finance had recommended, inter alia, a betterment charge upon “the granting of approval for development under a planning scheme, and any amendment, modification, or suspension of a provision in a planning scheme”. Subsequently, against the background of a substantial backlog of sewerage works and estimates of the enormous expansion of public works expenditure required to meet the forecast growth of metropolitan Sydney, the Liberal-Country Party Government’s *Land Development Contribution Act 1970* and *Land Development ~ Contribution Management Act 1970*

jointly authorised the State Planning Authority to impose a 30 percent land value increment levy on specified land rezoned from rural to urban uses within the Sydney metropolitan region. The levy was on the assessed increase in land value between 1 August, 1969 and the date of its rezoning (subject to an adjustment downwards to allow for general price inflation).

Unlike the more traditional concept of a betterment levy as a general revenue tax, the Sydney levy was expressly designed to provide funds specifically for the urban works and services needed in the new urban areas that had been released from the Green Belt. However modest the arbitrary 30 percent rate, and however geographically limited though it was to Sydney's outer fringes and limited conceptually to rural/urban conversion, the basic logic of the Sydney levy was nevertheless impeccable. By 1972/73 it had yielded some \$9 million.

However, the scheme was abandoned, and the legislation was repealed in 1973, amidst controversy over the alleged impact of the levy on land prices at a time of severe housing land shortages. Much of the released land was held by a small number of vendors who were in a position to claim indemnity for the levy when selling to developers. The legislation was repealed just prior to a state election (in which a disaffected former member of one of the government parties campaigned for election on the sole platform promise of abolishing the State Planning Authority). The NSW Government, succumbing to state financial subservience, declared it would seek additional funds for urban expansion from the Commonwealth. The opposition Labor Party chose not to defend the legislation and acquiesced in its repeal.

In 1975, referring to the abandoned Sydney experiment, the final report of the NSW Planning and Environment Commission (the successor to the State Planning Authority) declared:

No government in Australia has yet been able to devise a politically viable betterment tax. The termination of the last betterment tax in New South Wales is probably too recent for the State Government to agree to the imposition of some form of betterment in the foreseeable future. Yet many would agree that it was successful as a tax, that it was relatively simple to implement, that it gained wide acceptance, and that it produced funds that were necessary to implement plans... the Commission believes that the possibility of introducing a similar type of tax should not be discarded (NSW Planning & Environment Commission, 1975: 98).

Earlier, in 1973, the first report of the Commission of Inquiry into Land Tenures appointed by the Whitlam Government had recommended the reservation, without compensation, of all future development rights to the Crown (thus avoiding all the enormous financial and administrative complications associated with the abortive 1947 English Act). The commissioners were Justice Rae Else-Mitchell, Professor Russell Mathews, and Mr Gerardus Dusseldorp, significantly the chairman of directors of Australia's largest property development company, Lend Lease Corporation. However the report and its recommendations did not survive the demise of the Whitlam Government.

The ACT betterment levy

The only current example of a betterment levy in Australia is that which operates in the Australian Capital Territory. After the emasculation of the leasehold system by the Gorton Government in 1970-71, applicants (to the ACT Supreme Court) for a change of lease purpose were levied 50 percent of the difference between before and after valuations of their land. Subsequently the levy was increased on a sliding scale up to 100 percent where a lease had been extant for less than five years. Access Economics produced "An Economic Assessment of Betterment Issues in the ACT" for the ACT government in 1992, and a commission of inquiry headed by Judge Paul Stein reported on various aspects of land administration in the ACT in 1995, affirming in principle the levying of betterment. The subject remains a contentious issue, however, and within the ACT government there have been intimations of practical and ideological concern about the levy. In late 1998 the government commissioned a report on the levy from ANU economist Professor Des Nicholls, who was asked to review the administration of the betterment system and its impact on investment in the ACT. Nicholls reported somewhat ambivalently in May 1999 (Nicholls, 1999).

As an object lesson in misconceived land administration the origin of the ACT levy is instructive. The essential justification for the adoption of a leasehold system in the federal capital territory (and the legitimate expectations of its proponents) lay not only in eliminating for incoming citizens the initial capital cost of residential, commercial and industrial sites but in recouping for the government the cost of building the national capital. Revenue from land rentals would increase with population growth and community development and the city could eventually become self-supporting. Thus the public authority would capture the unearned increment. It was believed that leasehold tenure would also facilitate city planning (at a time when sophisticated land use planning controls were still in their infancy).

There were persistent controversies: for example, about how and how many sites should be allocated at any given time; about how rents should be assessed; about the significance of premiums offered in a competitive market; and whether the transfer of leases (by speculators) should be prohibited until lessees had complied with the conditions requiring them to build. The one essential requirement, however, if the government's investment was to be recouped, was the regular re-appraisal of rents in keeping with increasing land values. And from the outset in Canberra this was not understood: it was decided that lease rents would be re-appraised at 20-year intervals, i.e. on the basis of land values prevailing at the end of every 20 years. In practice this meant that lessees paid a fixed rent for sites which became increasingly valuable over the 20-year period during which the Commonwealth as lessor was denied the increasing revenue it should have recouped.

A bizarre consequence of this was the introduction of land rates to make up the revenue shortfall. Ostensibly they were justified as a charge for municipal services analogous with the rates levied on *freehold* landowners as the primary source of revenue available to local government councils in the states. The analogy of course is false. Under a public leasehold system the levying of rates in addition to rent is a conceptual absurdity - under a leasehold system the availability of municipal services is one of the factors which should be taken into

account in assessing land rent. In Canberra, where there was no local government, the incongruity was compounded by the fact that any rate could only be arbitrary since Canberra's municipal accounts were not separately identified (as distinct from the "national capital" component of the city's establishment costs). Deciding upon the amount of such a rate was therefore at best only a matter of guesswork.

The situation came to a head in the late 1960s, culminating - in retrospect, probably inexorably - in what, in terms of leasehold administration theory, was an act of monumental folly. Following the Menzies Government's re-affirmation of commitment to a national capital and the establishment of the National Capital Development Commission, the 1960s saw rapid expansion and population growth and a consequential increase in Canberra land values. At the same time, the fixed rents of many of the existing leases were coming up for re-appraisal. After 20 years the rents of many residents' leases were about to increase dramatically overnight and become a political embarrassment. The Department of the Interior claimed that the difficulties in making the leasehold system work had become overwhelming, and in 1970 the Gorton Government abolished land rents, thereby conferring upon the existing leaseholders of Canberra an enormous windfall gift of revenue foregone by the Commonwealth. The extraordinary munificence of this was seemingly not fully appreciated at the time by the Australian community at large or by resource-starved state and local governments. A similarly outrageous travesty of resource administration would be repeated if the demands of some pastoralists in response to the Wik decision were acceded to (Holmes, 2000) and their pastoral leases were converted to freehold at no cost to themselves.

It was decided that (apart from revenue from the sale of future leasehold sites) the Commonwealth would henceforth obtain its revenue by increasing Canberra rates and by imposing a betterment levy when approved changes in use purpose clauses conferred land value increases upon leaseholders. In essence, if not in name, the ACT leasehold system was abandoned. Certainly the essential fiscal characteristics of a leasehold system were abandoned. Lease purpose clauses remain a means of land use control in Canberra but, while lease purpose clauses are inherent in broad-acre rural leasehold, in urban areas land use in zones or precincts is more appropriately regulated by town planning schemes than on a parcel-by-parcel basis (determined by application to the Supreme Court).

Elsewhere, for example in Johannesburg and other cities of the Transvaal, a direct betterment levy has been mandatory since the *Transvaal Town Planning and Townships Ordinance* of 1965 which provided that, upon the coming into operation of an approved town planning scheme, a local authority should "in the general interests of any development within its area levy a monetary contribution" to assist in meeting expenditure incurred in connection with a town planning scheme (including any payment of compensation). A record contribution in Johannesburg in 1982 was approximately \$A9 million levied in respect of a 6,000 square metre site rezoned from "single residential" to "business". Other countries, France, Taiwan, Singapore and South Korea have operated various land value increment taxes and development charges more or less akin to betterment levies.

The conditions precedent

Failure to capture the unearned increment in land values is a well-documented flaw in the current planning system since it renders virtually all land vulnerable to profit-motivated development regardless of its environmental significance. Thus in principle the logic of capturing all or part of publicly conferred betterment by a betterment levy is unassailable; and the necessary pre-conditions for implementing a levy are simple enough, namely:

- a quantifiable benefit/betterment conferred by a public authority;
- one or more identifiable private beneficiaries;
- a public agency able to quantify the benefit/betterment;
- a public mechanism for implementing a levy to capture all or part of the quantified benefit/betterment; and
- the political will to adopt and implement it.

In Queensland the Statewide valuation authority has the capacity to undertake annual, or more frequent, assessments of market value on a consistent basis using established criteria; and virtually all land in private possession or public agency use has a designated land use. Given the necessary pre-conditions, the public revenue implications of capturing the unearned betterment reflected in land values are compelling. In a submission to the (then) Industry Commission in 1992, the National Capital Planning Authority estimated conservatively that the betterment being forgone throughout Australia as a source of funding urban infrastructure and community services was in the order of at least \$300-400 million annually, equivalent to more than a million dollars per day in 1992 values. Given the same pre-conditions, there is no reason why the concept should be confined to land.

Limitations

A betterment levy has inherent limitations, however, and introducing a levy obviously has political implications. In the case of planning decisions, the difference between before and after valuations is unlikely to be an accurate measure of the actual increase in land values, since in many situations the change to a more intensive land use is likely to have been anticipated by the market months or even years in advance. Secondly, a betterment levy cannot work in reverse and compensate worsenment although if it captured betterment, a public authority would be better able to afford to compensate worsenment.

A third limitation is that a once-off betterment levy cannot recoup the betterment conferred by the non-specific provision of general public infrastructure and incremental community development. A small percentage of this benefit is currently recouped by annual local government rates. A bigger percentage could be recouped by an ongoing betterment levy. But would this be in addition to and parallel with local government rates, or should the proportion of public revenue raised by local government rates be commensurately increased?

The possibilities invite speculation. The political implications of betterment levies need to be kept in mind. While betterment levies to recoup the unearned increase in the value of private assets attributable to publicly provided infrastructure and public land use decisions are

morally and logically defensible, the introduction of betterment levies as an additional source of revenue might well, be popularly portrayed as a “new tax”; unless some other field of taxation were to be vacated.

Surrogate betterment levies

While betterment levies as envisaged by the early post-war planning legislation have never been implemented in Australia except for the Sydney experiment and currently in the ACT, throughout the post-war years the phenomenon of negotiated development contributions has evolved tentatively, pragmatically, and with increasing sophistication to a point where development contributions are in effect surrogate betterment levies.

Their evolution, and that of their English equivalent, “planning gain”, has been recorded elsewhere. Commencing with modest requirements upon land subdividers to provide road access and dedicate public garden and recreation space, development contributions were refined to an art form by the Brisbane City Council in the 1960s (and they helped to get urban Brisbane substantially sewerred). In 1967 they survived the State-appointed Bennett Commission of Inquiry into the BCC’s subdivision practices.

Development contributions were facilitated by a curious provision in section 33, the very long town planning section in the old *Local Government Act*, which prohibited infrastructure exactions *unless the development proponents agreed to them*. The Local Government Court (later the Planning and Environment Court) adopted “reasonableness” and “relevance” as yardsticks to measure the validity of disputed development conditions. Elsewhere, section 94 of the NSW *Environmental Planning and Assessment Act* became the most sophisticated legislative statement regulating the practice and defining the scope of development contributions. In Queensland, the *Integrated Planning Act* (IPA) now provides for “infrastructure charges plans” in parallel, in the case of major projects, with negotiated contributions authorised by the *State Development Act*

However, the rationale of development contributions has never been explicitly stated. Implicitly they reflect the awareness of hard-pressed public authorities that planning approval, particularly rezoning approval (whether or not it is now called rezoning), confers a substantial land value increase upon the land vendor/developer. Unlike a conventional betterment levy, however, the quantum of developer contributions is not explicitly related to the increase in land value measured by before and after valuations. In the UK, “planning gain” contributions to a wide range of community facilities and infrastructure tend to be negotiated on the basis of the estimated profitability of development proposals as distinct from the land value increases flowing from planning approval. This however requires commercial expertise not always available in-house among local government councils.

Like betterment levies, a once-off development contribution cannot capture the benefit conferred by general community development (although some development conditions have imposed an ongoing obligation such as the maintenance of subdivision roads). And, like betterment levies, development contributions cannot operate in reverse and compensate worsenment or injurious affection (although gaining the contribution of infrastructure may make public authorities less resistant to the notion of compensation).

Politically, development contributions have an advantage. They have operated for decades and, while the development industry is disposed to object in principle to the kind and

quantum of contributions, imposing development conditions cannot be portrayed as introducing a new tax.

In Queensland there are, however, some over-riding constraints. For more than thirty years the town planning merits of local government planning decisions in Queensland have incongruously been argued by lawyers and decided by District Court judges (in the Planning and Environment Court). Judicial attitudes towards the “reasonableness” and “relevance” of planning conditions are necessarily influenced now by the tenor of the *Integrated Planning Act* and its narrowly circumscribed view of community development and the scope for development contributions. Without substantial amendments to IPA, any attempts in Queensland to impose betterment levies or development contributions in order to achieve wider public objectives, such as natural resources management or, in urban areas, the provision of affordable housing for low income earners, are unlikely to survive judicial challenge.

By contrast, NSW has adopted “inclusionary zoning” to achieve a measure of social mix in major urban redevelopments. And, as reported in the *Sydney Morning Herald* of 22/5/02, the NSW Government is currently contemplating funding metropolitan transport infrastructure by way of “land value capture” or a “betterment tax” which “would allow the Government to cream off part of the capital gains that usually go to property developers’ pockets.”

As they stand, the convoluted infrastructure charges provisions in IPA stand in the way of a simple, transparent and defensible requirement for contributions to general community development (which town planning was once conceived to be all about).

Reviewing the present situation

Summing up to this point, some or all of a specific benefit conferred by government on identifiable owners of any land - urban or rural - ought in principle to be recouped, and can in practice be recouped, if not by the introduction of a betterment levy then by requiring development contributions from development applicants in the benefited area. Otherwise the benefit will merge with general community development, and a small percentage will be recouped over time by local government rates (paid to local government councils irrespective of the origin of the benefit).

In passing it should perhaps be noted that enabling legislation can provide that levies or contributions may be waived or reduced if it is publicly disclosed policy to encourage development of a particular kind or development in a particular location which would not otherwise be viable.

As for the applicability of betterment levies and development contributions to rural industries and the rural environment, levies and contributions have historically been associated with the provision of urban infrastructure in urban areas and with the provision of infrastructure such as railways, ports and employee housing for major mining projects in regional areas. It is less easy to visualise their application in established rural areas, except perhaps in the case of a major augmentation and reticulation of irrigation water. On the

other hand, in the case of new, hitherto undeveloped rural areas, the provision of road or rail access would be a publicly conferred benefit which would increase land values.

Capital gains tax may seem to cloud the general issue of levies and contributions. It is sometimes asserted that the unearned increment/windfall gain accruing from planning approval is currently captured by capital gains tax, in which case a betterment levy or contribution would amount to “double dipping”. This would only be true if the windfall gain is realised by disposing of the property by sale, in which case, even at the highest marginal rate, the tax would not exceed 47 percent. And, if the benefited property is retained for more than 12 months, the capital gain subject to tax can be discounted by 50 percent. Whether or not the benefited property is sold, the land value accretion has of course an ongoing inflationary impact upon the State’s economy.

The Greenhouse Factor

Into the situation which has hitherto prevailed, a new factor has now been added. At a recent but indeterminate time a component of the value of land resources to government has come to be separately identified, namely what can be described as the “Kyoto compliance value” of vegetation. Given the cost to government of Kyoto compliance, the State has a legitimate policy interest in maximising this value by curbing the clearing of both old and regrowth vegetation.

In other words, the clearing of vegetation is a loss of Kyoto compliance value to the State, whereas in most cases it benefits landowners pursuing urban or rural purposes and increases the value of their land. Logically, therefore, where permission to clear is henceforth granted by the State, it is arguably a specific benefit conferred upon identifiable landowners. Accordingly it ought to be recouped (e.g. by a levy or development contribution, or some other alternative if one exists).

On a broad-acre basis it should be possible to determine the Kyoto compliance value to the State of vegetation generally and apply it uniformly throughout the State-wide valuation system (without compromising its integrity), thereby enabling the betterment conferred on landholders by clearing to be sufficiently identified and quantified. Conversely, the value of retained vegetation could be quantified for the purposes of devising conservation incentives.

If it were to be introduced from some announced future base date, a betterment recoupment initiative would not involve any significant discrimination or inequity in future expectations or entitlements. The private benefit of past clearing could not be retrospectively recouped of course, but the benefit of past clearing would subsequently be reflected for sale, leasing or rating purposes in relatively higher land valuations. Conversely, the retention of vegetation would be rewarded by relatively lower land valuations. Replanting and reforestation deserve to be encouraged of course, and their reward would likewise be a lower land valuation, but they would not seem to warrant any additional incentive. Any ecological benefit would be insignificant in the short term. Existing areas of ecological valuable vegetation can always be preserved by acquisition and designation, and the preservation of

aesthetically and environmentally significant vegetation can always be a condition of planning approval of zoning for tourism and recreational development.

The difficult problem, of course, would be the arguably legitimate expectations of existing owners or lessees to clear land for a purpose, permitted and intended, at the time they purchased or leased. To the extent that an anticipated lawful economic use was negated, the loss of value would be measurable. On the face of it, such landholders would seem to have a persuasive claim to be compensated, in which case the recency of their acquisition of their properties would bear upon the persuasiveness of their claim and the quantum of any compensation, like the quantum of betterment in the ACT.

Compensation law and philosophy

The whole area of betterment and compensation, however, is a particularly difficult and ill-defined branch of law and public policy, both in Australia and elsewhere. In the case of betterment, no clear-cut rationale has emerged in relation to development contributions, or their English and American equivalents. As for compensation, no unambiguous principles have evolved in respect of compensating worsenment or injurious affection, except for general acceptance of liability for compensation on just terms, as enshrined in the Constitution, in the case of land actually acquired although even this can be hinged around with qualifications about the timing and circumstances of acquisition.

Betterment and compensation are often referred to in conjunction in town planning law, but they are separate concepts and there is no necessary inter-relationship. What can be said, after viewing the chequered history of both concepts in Australia and elsewhere, is that governmental attitudes towards compensation tend to be influenced by the extent to which betterment is not captured.

In varying degree all shades of political opinion have come to acknowledge the desirability of capturing at least some of the unearned increment in land values. For example, throughout the decade or so since the Goss Government committed itself to revising Queensland's planning legislation, commencing with the interim *Local Government (Planning and Environment) Act* in 1990 and then the drafting of the *Planning, Environment and Development Assessment Bill* (PEDA), which in turn was overtaken and subsumed by the Coalition Government's IPA, debate about providing some compensation for 'down-zoning' was coloured by awareness of the fact that landowners who gained planning approval for a more intensive use were recipients of uncaptured windfall increases in land value.

In other words, therefore, it could well be that more generous attitudes to compensation would prevail if betterment were captured. Conversely, of course, a more generous attitude towards compensation would no doubt make the introduction of a betterment levy more palatable. Be this as it may, the horse surely comes before the cart. In principle, unless the readily identifiable betterment conferred by the State on private beneficiaries is captured, by rates, taxes or levies, it is manifestly incongruous even to contemplate compensating private worsenment.

If public affairs were only so simple and straightforward. Responding to new and hitherto unfronted circumstances like global warming and the need to conserve vegetation raises difficult questions about the inherent sovereign powers of the State and the proper limits of *eminent domain*.

In the overall public interest the State may frequently exercise powers which fortuitously impact adversely on private interests. Regulatory restrictions imposed by a democratically elected government can be assumed to be in the overriding public interest. But some element of luck cannot be eliminated. Private property can never be immune from fortuitous impacts, ranging, for example, from cyclical economic conditions and fluctuations in commodity prices, to obsolescence resulting from technological innovation and the loss of passing trade arising from highway diversions. Whether an entitlement to compensation deserves recognition in any given circumstances is ultimately a matter of political judgment.

In town planning law a now well-recognised but essentially arbitrary precedent was established in Bingham's case. While it begs the question of whether any regulatory restrictions imposed in the overriding public interest ever warrant compensation, the decision certainly narrowed the range of regulatory restrictions at least in the land use planning arena which might otherwise appear to warrant compensation. It was held that planning restrictions such as those regulating lot sizes, setbacks, boundary clearances and building height - the so-called 'good neighbour' restrictions - restricted a landowner's rights but did not give rise to a claim for compensation. However, the convoluted provisions of the IPA in respect of compensation, particularly section 5.4.4, seem likely to invite litigation in this regard. They appear to contemplate an entitlement to compensation if these kinds of planning restrictions reduce the yield of proposed developments.

A somewhat circumscribed entitlement to compensation for worsenment resulting from down-zoning existed in the old *Local Government Act*. The fact that this precedent survives in more specific terms in IPA, which in effect provide for the negotiated avoidance of worsenment within certain timeframes, derives in part from Queensland's distinctive attitude towards planning and zoning exemplified by the long-established practice of providing for private landholders, as well as councils, to initiate rezoning, now described as a 'material change of use'. There is of course some scope for negotiation in virtually all land use planning circumstances. About the only conclusion to be drawn is that Queensland planning law does not provide any very coherent or useful precedents for determining compensation policy in other areas of public administration.

Such, then, is the prevailing context in which any policy decision will have to be made about whether to compensate landholders for being prevented from clearing their land. The 'good neighbour' precedent tends to reinforce a narrow view of compensation. If clearing were likely to damage a neighbour's land, then of course a restriction upon clearing should certainly not attract compensation.

Short of special purpose grants, funded perhaps from a State-wide betterment levy, the only compensation, or consolation?, available to landholders affected by tree clearing restrictions will be a future reduction in their municipal rates flowing from a lower valuation of their land. But reduced rates, as research undertaken as part of the Skitch report (2000) indicated, will not be very significant as compensation - or as a positive incentive to conserve

vegetation. The problem of course is that, while the difference in valuations could be significant, municipal rates capture only a small percentage of land value. Landholders subject to State land tax would also benefit marginally from reduced valuations, and in some cases their reduced valuation might take them below the land tax threshold.

Municipal rates levied on the annually re-assessed value of unimproved land automatically capture betterment and compensate worsenment; and, unlike a once-off betterment levy or a once-off award of compensation, they do so on a continuing basis. And the compliance cost to ratepayers is virtually nil. But, at a few cents per dollar of assessed land value, they capture betterment or reflect worsenment only to an insignificant extent each year. As a footnote to any discussion of local government rates, it should perhaps be emphasised that the incentive potential of local government rates applies only in the case of rates levied on land alone - 'property rates' levied on land plus the improvements on it penalise the latter and operate as a disincentive to productive land use.

While they are a major source of local government revenue, municipal rates constitute only about five percent of total Australian public revenue. If more public revenue were raised in incremental stages by increased land value taxation, the problem of recouping betterment without a special levy and awarding compensation, without special purpose grants, would certainly be reduced. Other tax bases could be commensurately vacated, such as taxes on income, capital and labour which, as the European Union has acknowledged, tax what people add to the community rather than what they subtract by consuming the community's finite resources.

A charge upon the use of land is indeed a true consumption tax, unlike a GST which is a tax on the production and sale of goods and services at their point of sale. Economists from Adam Smith onwards have acknowledged that taxing land is the most logical and least distorting form of revenue raising, and there is no reason in principle why the consumption or use of other natural resources could not be similarly taxed if their value, not their area or volume, can be assessed. An obstacle of course is the current apportionment of revenue raising responsibilities between the three levels of Australian government. The Commonwealth has not levied a tax on land since 1952, and State land taxes are only a discriminatory wealth tax levied on arbitrarily determined property owners. Local government rates are the only true form of land value taxation, but the State derives no direct benefit from the limited amount of betterment which local government rates capture annually. Increased reliance on land and other community resources as a revenue base would certainly open up attractive possibilities for genuine taxation reform, beyond, however, the scope of the present paper.

Differential rating by individual local government councils is an option. Differential rates in favour of vegetated properties would accentuate the fiscal incentive deriving from their lower valuation. But locally administered differential rating on a property-by-property basis sits uneasily with a State-wide valuation system, and almost inevitably it would be subject to ill-attuned local pressures.

Some American literature canvasses the possibilities of using the mechanism of transferable development rights (TDR) to offset the impact of regulatory restrictions upon landholders; in other words by allowing the land use rights denied to be transferred and added on to the

development rights of other land held by the affected landholder, or sold to other landholders in a position to use them. TDR has some application in urban areas, for example in order to preserve low-level heritage buildings on sites which would otherwise be eligible for much more intensive development. But it is not easy to contemplate its usefulness in relation to rural land uses. And TDR invites awkward questions about the validity of land use planning limits on the receiving sites if they can be relaxed to the extent of permitting significant additional development.

Land nationalisation and nation-wide leasehold tenure is theoretically an all-embracing panacea, but an administratively daunting one apart from being politically unthinkable. Planning controls are now sufficient to regulate land use regardless of tenure; and the distinction between freehold 'ownership' and leasehold would gradually become less if, as suggested, a greater proportion of public revenue were derived by levies or rates and charges from possession of land. Meanwhile there is no reason to abandon existing agricultural and pastoral leasehold if it carries a right of renewal and reinforces land use control in rural areas. Like industrial leasehold in urban areas, it enables the user to avoid the capital outlay of freehold ownership.

Conclusion

Several main points have emerged from this paper. To sum up:

In principle, the capture by the State of betterment created by the State is morally and logically imperative in the interests of efficient and equitable public administration and rational resources management.

The retention of unearned betterment by private individuals is morally and logically indefensible.

Betterment currently being forgone by the State is a massive potential revenue source which could be applied to the further provision of public infrastructure or to achieving other public policy objectives.

Land value increases area measure of the betterment conferred by public works and services and public land use planning decisions.

If the beneficiaries can be identified, a betterment levy imposed on the before-and-after increase in land values is one administratively feasible method of recouping identifiable betterment from the occupiers of land.

Now that vegetated land has an acknowledged greenhouse value to the State, permission to landholders to clear vegetation is a measurable land value benefit or betterment which could be recouped; and uncleared land should henceforth have a commensurately lower valuation.

The levy imposed in Sydney in 1970-1973 raised significant revenue, but the only current example of a betterment levy in Australia is that in the ACT.

In the absence of betterment levies, infrastructure contributions extracted from land developers have in effect captured part of the unearned increment in land value, but their rationale has never been explicitly stated and the quantum of betterment has never been specifically related to the increase in land value resulting from planning approval.

As presently drafted, the *Integrated Planning Act* does not provide for betterment levies or for development contributions to community facilities other than the infrastructure narrowly defined for the purposes of 'infrastructure charges plans'.

As with betterment, land values likewise reflect worsenment or injurious affection resulting from public action.

Whether there are any circumstances in which worsenment attributable to regulatory restrictions imposed by the State in the over-riding public interest warrants some measure of compensation is a matter of political judgment.

It is conceptually very difficult to contemplate compensation by the State for worsenment while betterment conferred by the State remains substantially uncaptured.

Queensland town planning law does not provide an unambiguous guide to formulating compensation policy in other areas of public administration.

Once-off betterment levies or development contributions do not capture betterment on an ongoing basis. Nor can they operate in reverse to compensate worsenment. Revenue raised from recouping betterment by a levy or by development contributions could fund compensation if the circumstances of the worsenment were considered to warrant it.

Annual UCV-based municipal rates automatically recoup betterment including general community development (and automatically compensate worsenment), but only to a relatively insignificant extent.

If more public revenue were raised (at negligible compliance cost) by taxing the possession or consumption of land (or other natural resources), a greater proportion of betterment could be automatically recouped without recourse to a betterment levy.

Charges upon the possession or consumption of natural resources are the least distorting form of public revenue raising.

Whether by way of specific levies or development contributions or by land value taxation, recouping betterment would not require any departure from the principles of, or modification of, the existing State-wide land valuation system.

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