

## **IMPROVING HERITAGE SURVIVAL IN NEW ZEALAND A MARKET PERSPECTIVE**

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Economics of Heritage Conference, Canberra, October 2007**

### **Introduction**

The Australian Productivity Commission report “Conservation of Australia’s Historic Heritage Places” (2006) identified a number of significant issues that are fundamental to heritage management. In particular, the report acknowledged that the non-exclusive and non-rival nature of the property rights involved creates a market failure that is likely to lead to under-investment in heritage conservation. Secondly, their report observed that the usual forms of regulatory intervention whereby owners are obliged to protect the public heritage value of their property in order to overcome the market failure, in many cases simply reverse the property rights to change one form of market failure into another. The owner is forced to internalise the costs of providing the public good without the opportunity to capture the value.

The Productivity Commission was critical of this outcome and recommended that legislation providing automatic protection to listed properties should be removed from State legislation.

The Commission suggested that the more appropriate form of intervention is for governments to directly fund the heritage externality. This raises valid questions as to the appropriate level of public investment in such incentive schemes of which there are many examples in various forms. As yet, few of these schemes have their budgets determined through any process of cost benefit analysis. A rigorous process would take into account the opportunity costs of all other forms of social investment in order to determine an optimal level of public investment in heritage.

Determining the welfare maximising level of such investment pre-supposes that that we understand and can accurately measure both the public and private costs and benefits of heritage conservation at a micro-economic level.

As a non economist, there is little I can contribute to the detailed discussion of these techniques, other than making some minor observations about the political frame of reference in which these matters are considered and one market based technique that we have used to justify additional Government investment in heritage properties as tourist destinations.

Beyond that, I have largely eschewed the accepted wisdom of an incentive based approach and made some comment instead on a market based approach to land use regulation that offers an alternative means of addressing the externality.

### **Establishing Optimal Levels of Public Investment**

The determination of surrogate values for the purposes of cost benefit analysis, are beneficial in one important respect. That is to the extent that these methodologies establish that heritage has sufficient value to justify some form of intervention. The case is not always easily made.

That said, the methodologies do not seem sufficiently well developed, at least in the heritage sector, to provide a credible business case for a particular level of public sector investment in heritage. What is more, they often fail to reflect the reality that the allocation of public sector resources to outcomes such as heritage, occur at the margin. They are therefore influenced by macro-economic thinking about overall levels of government expenditure and competitors for the marginal government dollar.

Conventional wisdom in New Zealand holds that prudent economic management requires Government spending to be held at around 30% of GDP. Additional spending of increases in Government revenue is therefore likely to be limited by rates of economic growth and is purely contestable as between votes.

Fiscal pressure in New Zealand continues to be driven by increasing demands to provide both additional health care and superannuation benefits to an ageing population. Additional heritage dollars are being compared against the values associated with reducing hospital waiting lists, or keeping superannuation up with inflation. Nowhere is the process of government resource allocation more politically driven than at this margin. Surrogate values tend not to be well received in this space.

One relatively obvious approach the New Zealand Historic Places Trust (NZHPT) has employed to value heritage and thereby support a case for additional government investment, is a simple commercial model which demonstrates the potential return on Government investment in heritage properties to the tourism sector.

Basic studies undertaken by Tourism New Zealand have documented the dollar value of domestic and international visitor spend per day in the Northland region. From this NZHPT has been able to calculate both the net national benefit and the regional economic benefit, expressed as Net Present Values and Benefit - Cost ratios, that would be derived when additional Government investment at defined levels in key heritage properties results in an increase in the number of overnight visitor stays.

It is questionable whether these numbers could be considered as surrogate values for the continued existence of heritage places, however they do have the benefit of commercial reality and in the limited context from which they are derived, are a measure of willingness to pay.

## **The New Zealand Context**

Functions of the New Zealand Historic Places Trust / Pouhere Taonga (NZHPT) include:

- Regulatory control over the disturbance and investigation of archaeological sites.
- Registration of significant historic places.
- Provision of heritage advice to the public and government.
- Statutory advocacy under the Resource Management Act for the protection of heritage places.
- Assistance and advice to Maori on the conservation of Maori built heritage.
- Management of 45 nationally significant heritage properties ranging from cathedrals, bridges, lighthouses, pa sites, houses, commercial buildings, farm buildings, industrial archaeology sites, and military redoubts,
- Administration of a government heritage preservation incentive fund.
- Providing services to and representing our members.

Our mission is the identification, promotion and protection of historic heritage in New Zealand.

NZHPT is funded from Vote Arts, Heritage and Culture with the corresponding Minister. In addition to our 100 staff across seven offices we have a Board of Trustees, A Maori Heritage Council, 26,000 members and 24 Branch Committees.

NZHPT is a somewhat unusual organisation in that it combines in one national organisation, most of the responsibilities for the management of historic places that in other countries are separated. Regulatory control over built heritage (other than archaeology) however is the responsibility of Local Government under the Resource Management Act.

The legacy of New Zealand's neo-liberal economic reforms of the 1980's means that the New Zealand heritage regulatory environment looks very much like Australia's Productivity Commission had already paid a visit.

With one very minor exception, listing (registration) of a property by NZHPT does not provide automatic protection. The process of registration under our Historic Places Act must be followed by a separate process leading to inclusion of the property in the regulatory schedules of a Territorial Local Authority's District Plan under the Resource Management Act (RMA). This regulatory hiatus is often exploited by developers who are able to demolish before the protection of scheduling under the RMA can take effect.

Property owners have the right under the RMA to be heard in support of or opposition to such proposed regulatory controls and to appeal decisions to the Environment Court. There is also the ability under the RMA for the Environment Court to strike out controls that prevent an owner from enjoying a reasonable economic use of their property. This power is rarely exercised as the test requires almost no possible economic use and the RMA authorises regulations for a variety of social and environmental outcomes that limit the economic potential of real property.

There is also a requirement in Section 32 of the RMA that proposed regulations must be subject to an evaluation of the extent to which, having regard to their "efficiency and effectiveness" the proposed policies and rules are the most appropriate for achieving the objectives. This test is largely ignored at all but the most basic level of analysis, but it nevertheless creates a presumption. Combined with the opportunity for relatively low cost challenge to proposed controls, it does require that consideration be given, albeit in a politico-legal framework, to the allocation of costs and benefits and to the relative equity and efficiency of the outcomes.

The absence of automatic protection for listed buildings therefore requires some up-front justification of the proposed controls by defining the benefits and demonstrating that the allocation of costs have been considered. The process also creates incentives to reduce the size of the externality. It is this area that offers significant opportunities to improve heritage survival rates at reduced cost to both private land owners and to communities.

### **Limitations on Listing as a Means of Improving Heritage Survival**

As public interest in heritage increases there are more frequent calls for regulation to ensure the survival of individual properties and increasingly to protect the characteristics of whole neighbourhoods. It is not surprising that the rights of the owners of these properties are also becoming a contentious political issue.

In recent years and with a number of well publicised failures to protect significant heritage, NZHPT has reached the view that listing under our Resource Management Act, while necessary to protect the most significant heritage, is no longer sufficient to encourage the retention of all of the heritage places that warrant some form of intervention. Two factors have driven this conclusion.

First, the extent to which listing relies on individuals facing the costs of providing public goods means that techniques such as listing or scheduling are not politically capable of widespread use. NZHPT is very much aware of the fact that most of the heritage we seek to protect is in private ownership. In contrast to natural heritage, the subject of our attention is often a family home or if business premises, someone's livelihood.

Second, the inability to intervene on all but the most significant listed properties often requires heritage organisations to fight last minute battles for un-protected properties using media and political pressure to generate the funding or the regulatory will-power to achieve protection of an important heritage place. Success will generally however be limited to just one piece of heritage, and while it may generate a public profile and gain more members, the gains are marginal, and the overall public perception is often negative.

In most cases heritage organisations have tended to rely on listing because there are inadequate financial resources to incentivise conservation or to purchase. While both central and local government have strong preferences for the use of incentive based measures the antipathy towards paying from them is just as strong.

The current raft of interventions available is therefore limiting our ability to improve heritage survival rates. If we are to ensure the conservation of the heritage NZHPT considers justifies and requires intervention, new techniques that are more equitable as well as being effective and efficient, are required.

### **Interventions that Modify Incentives**

A different approach recognises and relies on the fact that Government action has a great deal of influence on land value. City Planners have been using land use regulation to influence value and incentivise the retention or creation of public goods for many years. The minimisation or creation of land use options which limit market differentials with and without heritage can be both equitable and efficient.

The range of options being suggested here all have one thing in common. They require that the public heritage values to be conserved and the sites with which they are associated are identified early and clearly.

In our case the Register as a national inventory of significant historic heritage needs to be robust and comprehensive. It should clearly establish, rank and publicise the sites that are considered to be of significant heritage value. It does not yet meet these criteria but changes are being made that will address these shortcomings.

### **Identifying and Understanding Risk Drivers**

Understanding the financial drivers that place heritage sites at risk is a key requirement of determining appropriate intervention to encourage their conservation.

There are a number of common heritage risk drivers:

- Information failures mean that the owner may not be aware of the heritage value of the place and would voluntarily protect it if he or she was made aware of these values.
- Market failure may mean that the heritage values, by virtue of their non exclusive and non rival nature may not have sufficient market value to warrant private investment in protection therefore the values are not reflected in re-investment decisions.
- The building may have reached a physical state whereby significant re-investment is required to continue its use and/or to meet regulatory standards (e.g. earthquake strengthening or public health) but the cost cannot be recovered in its current use or within its current floor plate.
- The value of the underlying land may have escalated to the point where the heritage building or current use of the site, may be incapable of generating a commercially viable rate of return. Demolition followed by the construction of a larger floor plate, or a change of land use which threatens heritage values, may be necessary to achieve this.

The last two factors are not market failures but exacerbate the effect of market failure by widening the gap to market value. A combination of these factors is common.

In the first case, intervention in the form of education will often suffice. In the remaining three situations, regulation would be supportable provided a reasonable economic use may still be made of the property. However this will continue to leave the owner in a position of economic

disadvantage where the regulation is applied retrospectively. Other forms of intervention are available that improve the prospects for heritage survival.

### **Preventing Market Differentials**

The first approach is to prevent market differentials from arising in the first place.

It is possible to reduce the gap to market through early intervention to influence land value. These methods can be used to either increase land value or suppress it.

The key to the equity and efficiency of these interventions lies in the timing of their use. The nature of the heritage values and any consequent restrictions should be made clear to current owners and prospective purchasers well in advance of any market driven increase in land value.

The key to their efficiency also lies in the clarity with which restrictions on use are specified. Such clarity enables prospective purchasers to undertake due diligence, establish reasonably accurate valuations, and make appropriate investment decisions. Some examples of these forms of intervention follow, there are many others that are commonly used to incentivise the retention or creation of other forms of environmental quality:

- Land use planning controls can be used effectively to prevent large market differentials arising where heritage values are known to exist. Trends that are likely to give rise to market differentials are not difficult to identify and are controllable under most land use planning regimes. These include rural intensification, rural - residential transition (important for archaeological sites) and residential - commercial transitions.
- Another proactive measure only recently introduced in New Zealand is that of requiring all Government Departments, Crown Agencies and State Owned Enterprises to undertake a heritage assessment prior to the disposal of Crown Land. This enables the government to covenant or reserve significant heritage at a time when the cost of restrictions can be shared by the whole community. Purchasers take the land aware of the restrictions on its value and pay a price that reflects the restrictions on the title.
- One approach that has been used to good effect is for Councils to create special character zones which make a feature of the value to be recognised. This enhances market recognition of the value of the heritage characteristics and assists in preventing gaps from arising. In some cases, these forms of intervention have created a market premium for heritage. In one case I am aware of there is pressure to extend the boundaries of the zone from owners and investors keen to increase property value.

### **Closing Market Differentials**

Once a market differential has arisen the game is not over. A number of other interventions that incentivise retention of heritage are possible.

- Land use controls can also create significant opportunities for adaptive re-use. Specific uses can be identified and permitted for the site concerned that are compatible with the adjoining land uses but which permit a use of the property that will generate sufficient return to close the gap with the value of the underlying land. These provisions incentivise the retention of a building and investment in its ongoing use.
- Tradable development rights are another option that has been successfully used for the protection of amenity values that otherwise exhibit the same market failure characteristics. Plot Ratio allocations have been successfully used as a form of tradable development right for heritage buildings and could be more widely applied. The sale of

floor plate extensions are a means by which the owners of heritage properties are compensated for the public good they continue to provide and the development rights foregone.

- Rates rebates are a mechanism that is not generally favoured by Local Government however restrictions that protect heritage places are not always reflected in capital valuations but create a strong case for reductions or exemptions and require more explicit consideration.
- Incentive funds at both central and local government level are also increasingly being used to provide financial support to owners not otherwise able to afford the cost of re-investment. These mechanisms are limited by the depth of public pockets and always require a covenant requiring ongoing protection to be agreed as a condition of the assistance. They tend to be limited to the most significant and at risk sites.
- Acquisition of property by public bodies is normally considered as a last resort, however there are many successful examples around the western world of revolving funds being used to acquire, re-develop, covenant and on-sell, heritage properties at risk. There are several New Zealand examples where local community trusts and in one case a local authority have made an art form of this technique at relatively low cost. In one case turning the fund into a profitable business venture.

### **Financial Incentives**

Notwithstanding earlier comments about Governments' traditional unwillingness to fund incentive schemes, an impressive range of financial incentive techniques are possible and have the advantage of directly overcoming the issues raised by the Australian Productivity Commission.

- Incentive funds have achieved significant heritage conservation gains, both locally and nationally. The New Zealand National Heritage Preservation Incentive Fund, although relatively small, leverages significant private investment and is often used to assist in the retention of some of the most significant heritage at risk in private ownership.
- National loans schemes particularly in relation to commercial property requiring upgrades to meet building code standards (particularly for earthquake strengthening in New Zealand), are also worth of investigation. The capital sum required to underwrite and administer the loan scheme could be funded from building consent levies.
- Tax deduction/tax credit regime for conservation (including repair, maintenance, earthquake strengthening and fire protection systems) for revenue-generating and privately-owned registered and/or listed properties are also possible. Such schemes are in widespread use in many jurisdictions.
- Tax deduction/tax credit regimes for donations to approved conservation projects on registered and/or listed properties and to national, local and community heritage conservation organisations and groups is another option.

All such schemes often face opposition by Treasuries to the principle of hypothecated taxation.

- Not to be overlooked as a form of incentive and as a means of addressing information failures is the availability to owners of registered and/or listed properties of free heritage advice and assistance from organisations like the NZHPT and local authorities. Assistance with advice as to adaptive re-use opportunities and specialist technical advice, has regularly proven to be all that is required to ensure the survival of heritage places.

## **Conclusion**

New Zealand is at an early stage in the development of model provisions for our second generation of land use plans under the Resource Management Act. In developing these plans we are recognising that the current forms of regulatory intervention commonly used are not sufficiently equitable or efficient to be capable of application to the range of places with heritage values that warrant some form of intervention to ensure their survival.

NZHPT is encouraging Councils to recognise that there are a number of forms of intervention available that incentivise the retention of heritage by reducing both the market and market failure driven differentials that traditionally put heritage at risk.

New approaches of the type described in this paper are required if the places that help to define us as a people, that give a sense of place, of belonging, and that contribute to our social cohesion are to continue provide us with the benefit of their symbolism into the future.

## **Bibliography**

Productivity Commission 2006, Conservation of Australia's Historic Heritage Places, Report No. 37, Canberra Australia.