



**STATEMENT OF EVIDENCE OF DANIEL STEVEN NEWMAN  
TO THE CANTERBURY EARTHQUAKES ROYAL COMMISSION**

**INTRODUCTION**

1. Thank you for the opportunity to appear before the Canterbury Earthquakes Royal Commission (the **Commission**). This hearing provides an invaluable opportunity to examine issues in the Christchurch central business district.
2. My name is Daniel Newman. I am the Policy Director for Property Council New Zealand (**Property Council**). I am a graduate from the University of Auckland, where I gained a Bachelor of Arts and a Master of Arts degree in Geography. I have worked in public policy development and analysis since 2000. I have been employed as the Property Council's Policy Director since 2005.

**BACKGROUND - PROPERTY COUNCIL**

3. Property Council is a not for profit organisation that represents New Zealand's commercial, industrial, retail property funds and multi unit residential property owners. Property Council represents all forms of commercial property and property investment. Property Council's members collectively own and manage \$30 billion of commercial property investment in New Zealand.
4. Property Council is actively involved with central, local and other government associated bodies. It promotes the views, goals and ideas of its members. In October 2011, Property Council made submissions on the report titled "*The Performance of Unreinforced Masonry Buildings in the 2010/2011 Canterbury Earthquake Swarm*" co-authored by Associate Professor Jason Ingham and Professor Michael Griffith (**Ingham and Griffith Report**). We address the particulars of that report later below.

5. Property Council supports excellence within the built environment. Our organisation is a signatory to the Urban Design Protocol. We are generally supportive of the Green Building Council of New Zealand and applaud excellence in design and construction. We also support a public policy environment that is sympathetic to the delivery and maintenance of that type of building works.
6. Property Council supports the need for a safe built environment in New Zealand and deplore the loss of life that has occurred in Canterbury. In addition to the 182 people who died, many others were deeply affected (physically, emotionally and financially). Homes and livelihoods have been destroyed. Many parts of Christchurch will not be rebuilt.
7. Although Property Council is not able to provide evidence that directly relates to the Commission's inquiry into the Canterbury Television, Pyne Gould Corporate, Forsyth Barr or the Hotel Grand Chancellor Buildings (**Specified Buildings**), we commend the Government's decision to establish Terms of Reference that require the Commission to examine the failure of those buildings.
8. Property Council supports a regulatory regime for the built environment that promotes public safety and which minimises the risk of loss of life. Property Council supports practices that promote the construction (and maintenance) of buildings that are safe, efficient, enhance the character of the built environment, and which are economically viable.
9. The 2011 Human Development Report commissioned by the United Nations Development Programme, recently rated New Zealand fifth in the world in the annual Human Development Index. Relative to other countries, New Zealanders live long and healthy lives, have access to knowledge, have one of the best education systems in the world, and enjoy a comparatively favourable standard of living (measured by Gross National Income).

10. Property Council is concerned about the adequacy of Schedule 1 of the Building Regulations 1992 (the New Zealand Building Code) (**Code**) and standards. Property Council looks forward to contributing to debate relating to the regulatory regime affecting the built environment, both now and for the future.
11. Property Council wishes to present its submission relating to the legal and best-practice requirements for the design, construction, and maintenance of buildings in central business districts in New Zealand.

## **TERMS OF REFERENCE**

12. It is not possible for Property Council to comment on the issue of why the Specified Buildings failed. It is also not possible for Property Council to comment on matters that address issues such as the land associated with the buildings, or previous certification and consenting issues involving the Christchurch City Council.
13. However, this Commission has wide Terms of Reference, which allows it to examine the legal requirements for buildings that are “earthquake-prone”. The Terms of Reference include inquiring into the extent to which existing buildings are, and should be, required by law to meet requirements for the design, construction, and maintenance of new buildings; as well as the enforcement of legal requirements. It is on these issues that the Property Council seeks to be heard

## **STATUTORY REQUIREMENTS – BUILDING ACT 2004**

14. When dealing with existing buildings, there are a number of relevant sections of the Building Act 2004 (**Act**) that need to be considered in relation to the structure and strength of a building.
15. Section 112 of the Act deals with the Alteration of Existing Buildings. It requires that a building consent must not be granted for the alteration unless the building consent authority is satisfied that after the alteration, the building will comply with the provisions of the Code. This essentially means a building may not be made any weaker than it was, as a result of any alteration.

16. Section 115 of the Act deals with Change of Use. It requires that the territorial authority (in this case the Christchurch City Council) be satisfied that the building in its new use will comply with the relevant sections of the Building Code “as nearly as is reasonably practicable”.
17. Section 131 of the Act requires all territorial authorities to adopt a specific policy on dangerous, earthquake prone, and unsanitary buildings.
18. Property Council understands from the Council’s Earthquake- Prone, Dangerous and Insanitary Buildings Policy 2010 (**Policy**) that in relation to a building’s earthquake strength, this section will be interpreted as requiring earthquake strengthening to a minimum level of 67 per cent of that required for an equivalent new building.
19. Section 122 of the Act deals with the Meaning of an Earthquake Prone Building. It deems a building to be earthquake prone if its ultimate capacity (strength) would be exceeded in a “moderate earthquake” and it would be likely to collapse causing injury or death, or damage to other property. For the purposes of section 122, Regulation 7 of the Building (Specified Systems, Change of Use and Earthquake-Prone Buildings) Regulations 2005 define a moderate earthquake as one that would generate shaking at the site of the building that is of the same duration as, but that is one-third as strong as, the earthquake shaking that would be used to design a new building at that site.
20. Section 124 of the Act deals with the Powers of Territorial Authorities. It states that if an existing building is found to be earthquake prone, the territorial authority has the power under section 124 of the Act to require strengthening work to be carried out, or to close the building and prevent occupancy.

#### **CHRISTCHURCH CITY COUNCIL POLICY**

21. Property Council understands that after the Darfield Earthquake (in September 2010), the Christchurch City Council adopted (under urgency) the second version of its (**Policy**). Amongst other things the Policy has been amended to include a section

on the repair of buildings damaged by earthquake, as follows:

### **2.3.6 Buildings damaged by an earthquake**

*Buildings may suffer damage in a seismic event. Applications for a building consent for repairs will be required to ensure structural strength. The Council will follow sections 2.3.1 and 2.3.3 of this Policy in determining the level of strengthening required for each building.*

*If a building consent application for repairs is not made and/or the repair work is not completed within a timeframe that the Council considers reasonable the Council reserves the right to serve notice under section 124(1) of the Building Act 2004 to require the work to be done.*

22. Property Council understands that Section 2.3.3 of the Policy essentially requires that a building is required to be repaired to a level equating to 67 per cent of Code loading. The technical requirements for determining earthquake-prone status are done with reference to the New Zealand Society for Earthquake Engineering (**NZSEE**) guidelines, "Assessment and Improvement of the Structural Performance of Buildings in Earthquake".
23. The definition of an earthquake-prone building (as set out in section 122 of the Act) as having the capacity to resist a moderate earthquake (equivalent to 33 per cent current Code) is therefore directly related to the current design load level as required by the Code and Policy.
24. Property Council understands that the seismic design load levels for Christchurch have been increased as a result of the Darfield Earthquake. The Department of Building and Housing (DBH) have increased the Zone factor (Z) for Christchurch from 0.22 to 0.30 (a 36 per cent increase). This became official on 18 May 2011. This has implications regarding the strength of existing buildings (as a percentage of current Code) where a building is deemed to be earthquake-prone, or where works are

undertaken to require an alteration or addition, or change in use.

## PROPERTY COUNCIL SUBMISSION TO THE COMMISSION

25. In its 14 October 2011 submission on the Ingham and Griffith Report, Property Council made a number of points. As stated in paragraph four:

*Property Council supports the purpose of the Building Act 2004. Section 3 of the Act states that the regulation of building work, the establishment of a licensing regime for building practitioners, and the setting of performance standards for buildings is designed to ensure that:*

- (a) people who use buildings can do so safely and without endangering their health; and*
- (b) buildings have attributes that contribute appropriately to the health, physical independence, and well-being of the people who use them; and*
- (c) people who use a building can escape from the building if it is on fire; and*
- (d) buildings are designed, constructed, and able to be used in ways that promote sustainable development.*

*Ensuring public safety means designing and maintaining buildings that are survivable. The Building Code must enable building and design outcomes that protect against the loss of life.*

26. At paragraph 8 of the Submissions:

*Property Council believes the Commission should recommend to the Government that the review of the Code should be widened to include a review of section 112 (Alterations to Existing Buildings) and section 115 (Code Compliance Requirements: change of use) of the Act. Such a review*

*will require wide stakeholder participation given the significant financial implications of moving to a higher minimum standard against the Code.*

27. At paragraph 9 of the Submissions:

*The 2010 and 2011 Canterbury earthquakes have implications for the viability of both the Canterbury region and the wider New Zealand economy. Property Council supports changes to tax policy to facilitate improvements in the performance of buildings. These changes include:*

- *allowing an immediate deduction for (all or part of) the cost of rebuilding;*
- *allowing a special depreciation deduction for repaired/new buildings; and*
- *a permanent deferral of any depreciation recovered on new buildings.*

*The Report's recommendation that a single national policy for unreinforced masonry building maintenance and seismic strengthening justifies a national approach to tax reform as opposed to a change that is specific to Canterbury. Property Council would support a national approach to tax changes that facilitate improvements in the performance of buildings.*

*If a single national policy for unreinforced masonry building maintenance and seismic strengthening is to be introduced, it should only be in conjunction with a policy allowing the deductibility of earthquake strengthening expenditure. Historically, the treatment has been that such costs must be capitalised (effectively meaning no deduction arises with the removal of tax depreciation on buildings). Given the requirements of an increasing number of councils for buildings to be earthquake strengthened*

*to meet modern building standards, as well as the general “social good” element in doing such work, there are strong arguments for making these costs deductible. Such a recommendation to the Government would go some way to providing the “cost effective strategy” referred to in the Report.*

28. As set out above, Property Council supports practices that promote the construction (and maintenance) of buildings that are safe, that are efficient, enhance of character of the built environment, and which are economically viable. From the Commission we seek a series of recommendations to the New Zealand Government about the necessary steps to achieve those objectives.

#### **INTERIM RECOMMENDATIONS OF THE COMMISSION**

29. On 10 October 2011 (pursuant to the Order in Council dated 11 April 2011), the Commission issued an interim report (**Interim Report**). The Interim Report set out a series of recommendations which are relevant to current and future building owners, including the owners of Unreinforced Masonry Buildings (**UMB**).

30. While the Commission is still considering evidence made by interested parties, it has already recommended actions that should be taken as a matter of urgency, including:

*local authorities should ensure that registers of all URM buildings, their locations and characteristics, are compiled or, where they already exist, brought up to date; and*

*throughout New Zealand, URM buildings should be improved by bracing parapets, installing roof ties and securing external falling hazards in the vicinity of public spaces; and*

*in areas where the hazard factor in NZS 1170.5 is 0.15 or higher, additional steps to provide ties at all floors should be implemented, at the same time*



*as the work referred to in recommendation 6; and*

*these recommendations should be implemented as soon as practicable.*

31. Property Council endorses these recommendations. The need to minimise the risk of loss of life is paramount. New Zealand's built environment must reflect best practice and promote the construction (and maintenance) of buildings that are safe for people who use them.
32. The recommendations in the Interim Report reinforce the obligations on every territorial authority (pursuant to section 131 of the Building Act), to adopt a specific policy on dangerous, earthquake prone and unsanitary buildings.
33. Territorial authorities (post the Christchurch earthquakes) are grappling with their obligation to enforce provisions to enhance the performance of UMB. These debates have only just begun.
34. The Ingham and Griffith Report (as outlined in the Interim Report at page 38) recommend a four-stage improvement process for strengthening UMB as follows:

***1st stage:*** *ensure public safety by eliminating falling hazards. This is done by securing/strengthening URM building elements that are located at height (eg, chimneys, parapets, ornaments and gable ends).*

***2nd stage:*** *strengthen masonry walls to prevent out-of-plane failures. This can be done by adding reinforcing materials to the walls and by installing connections between the walls and the roof and floor systems at every level of the building so that walls no longer respond as vertical cantilevers secured only at their base.*

***3rd stage:*** *ensure adequate connection between all structural elements of the building so that it responds as a cohesive unit rather than individual,*

*isolated building components. In some situations it may be necessary to stiffen the roof and floor diaphragms, flexurally strengthen the masonry walls, and provide strengthening at the intersection between perpendicular walls.*

**4th stage:** *if further capacity is required to survive earthquake loading, then the in-plane shear strength of masonry walls can be increased or high-level interventions can be introduced, such as the insertion of steel and/or reinforced concrete frames to supplement or take over the seismic resisting role from the original unreinforced masonry structure.*

35. The Ingham and Griffith Report at paragraph 5 on page 115 states that:

*The estimated cost to upgrade all 3867 URM [Unreinforced Masonry Building] buildings in New Zealand to a minimum of 67% of the NBS [New Building Standard] is roughly \$2.1 billion, which is more than the estimated total value of the URM building stock of \$1.5 billion. However, a multistage retrofit improvement program has been recommended and it is anticipated that the cost of implementing stage 1 and stage 2 improvements will not be excessive and should be within the budget capability of most building owners.*

36. There is currently debate about how this process going to work and how New Zealand will arrive at a situation whereby we have the ways and means to improve the performance of UMB, and what public policy changes are necessary to deliver that outcome

37. It is not possible to accurately assess (for the purpose to today's hearing) the actual cost of upgrading all of New Zealand's UMB. It also not possible to anticipate whether in fact staged improvements will be within or in excess of the budget capability of affected building owners in New Zealand. This is the challenge that confronts this Commission, every territorial authority, the Department of Building

and Housing, the New Zealand Government, and the owners of UMBs.

## **DEPRECIATION AND THE COST OF BUILDING MAINTENANCE**

38. In 2009 the Tax Working Group posed a series of questions and researched the appropriateness of various tax reforms. The Tax Working Group's analysis and recommendations was a key driver in persuading the New Zealand Government to make a series of tax changes in Budget 2010. The Budget 2010 tax changes included removing tax depreciation on buildings (including commercial and industrial property), although as I discuss later this appeared to be more for pragmatic rather than principled policy reasons.

39. In its advocacy to the Government in the lead-up to Budget 2010, on tax issues Property Council reiterated that:

- a. Buildings do depreciate, at least in the context of non-residential buildings (e.g. commercial and industrial property, which was the focus of Property Council's analysis);
- b. International evidence, including the various economic studies since the late 1970s concluded that commercial and industrial buildings broadly depreciate at rates of between 2 - 4 per cent each year. These studies were noted in an Inland Revenue and Treasury issues paper on tax depreciation, released in 2004, which concluded that tax depreciation should not be removed.
- c. More recent international evidence also supports the officials' 2004 analysis, with these studies suggesting that depreciation rates for commercial and industrial buildings could be higher (coupled with that, the useful lives of buildings appear to be shortening). Importantly Property Council did not find any studies that suggest buildings do not depreciate.
- d. If the New Zealand Government were to deny depreciation deductibility for buildings, New Zealand would be an outlier internationally. We noted that the majority of our trading partners, including Australia, Germany, Japan and

the United States allow depreciation on (some or all) non-residential buildings. In the race to attract and retain capital, we noted that New Zealand would be at a significant disadvantage.

- e. Qualitative factors, such as: the high-rates of re-development of commercial buildings (particularly in the Auckland and Wellington CBD areas); changes in building technology (i.e. the need to comply with new building standards); and changing tenant preferences (i.e. “Green” buildings for Government and changes in configuration over time, due to the move from individual offices to open plan) mean that buildings can and do economically lose value over time. Buildings also move across different segments of the market, over their economic life reflecting deterioration in income-earning capability (e.g., a prime building in the 1970s will typically be sub-prime property today, all other things held constant).
- f. The economic cost of removing depreciation on buildings would be borne primarily by the New Zealand business sector and non-residential building owners. This was based on a breakdown of what property Council understood then to be a \$1.3 billion revenue gain from removing depreciation. We understood approximately 70 per cent of this estimate related to non-residential property depreciation, making it difficult for the New Zealand Government to meet its other tax commitments while excluding commercial and industrial property from the scope of any change (particularly as the revised revenue estimate was significantly lower than the original, providing Ministers with even less room for manoeuvre in excluding non-residential buildings).
- g. The flow-on implications from removing the right to claim for depreciation on buildings would be lower quality of infrastructure (as there would be lesser incentives to reinvest capital) or higher rents (as landlords look to recover the lost tax deductions).

40. The reason why this commentary is important is it relates specifically to public policy

decisions that were taken in 2010 which in Property Council's view now significantly constrain the ability of property owners to fund changes to their buildings. In effect, any additional work to the building structure is not deductible or depreciable, resulting in an additional cash cost to building owners.

41. Depreciable property is defined in the Income Tax Act 2007 as *"property that, in normal circumstances, might reasonably be expected to decline in value while it is used or available for use in [either] deriving assessable income; or in carrying on a business for the purpose of deriving taxable income."*
42. A number of the international studies that Property Council analysed separate out the depreciation attributable to physical wear and tear (i.e. the deterioration in physical capacity of the building asset) with so-called economic depreciation (which relates to the ageing of an asset and is attributable to factors such as obsolescence). Depending on which type of depreciation is being discussed, the economic profile of loss in value may vary.
43. Property Council's definition of depreciation – which was articulated to Inland Revenue and Treasury officials advising the New Zealand Government – emphasised the role of economic depreciation. As noted above, environmental factors can include changes in building technology, i.e. obsolescence, as well as changes in tenant preferences such as the configuration and internal specification of a building, which will affect a property's value over time. Property Council submitted that it is this "economic" definition of depreciation that Ministers should have regard to.
44. Notwithstanding Property Council's (and others) submissions, in Budget 2010 the New Zealand Government announced a policy change denying depreciation deductions for buildings, such as rental housing and office buildings, with an estimated useful life of 50 years or more. This policy announcement took effect for all such buildings from the start of the building owners' 2011/12 income year.
45. In no way is Property Council suggesting that the buildings that failed during the Canterbury Earthquakes did so because of a public policy change relating to denying

depreciation deductions. Many of the buildings that failed had stood for many decades, and it is the responsibility of the Commission to inquire into the reasons for building failure.

46. But it is nevertheless important to consider how the taxation rules may impact adversely on New Zealand property owners undertaking improvements in the future. From that perspective, Property Council submits a series of proposals for the Commission's consideration, which in our view should constitute recommendations to the Government:

- a. Depreciation on non-residential property classes should be reintroduced to reflect the reality that buildings do in fact depreciate over time.*
- b. New Zealand should sit within the mid-range of OECD countries in terms of the application of depreciation for non-residential property classes in order to compete for internationally mobile capital.*
- c. If the above recommendations are not accepted, at a minimum there should be scope for losses on buildings (e.g., on sale or demolition) to be claimed. Currently losses can only be claimed in limited circumstances.*
- d. The 2010 and 2011 Canterbury earthquakes necessitate a new approach to the taxation treatment of earthquake strengthening. Historically, earthquake strengthening has been treated as a capitalised cost (effectively meaning no deduction arises with the removal of tax depreciation on buildings). The cost of strengthening buildings to mitigate earthquake-related damage or loss should be deductible to reduce the financial burden of this building work on individual property owners.*

*e. The timing of Canterbury's recovery is uncertain. The lack of momentum is unacceptable given the size and significance of Canterbury as a regional economy. Property owners should be allowed to claim an immediate deduction for (all or part of) the cost of rebuilding. The Government should be prepared for a clear, direct path for the rebuilding of Christchurch.*

47. Property Council hopes the wide Terms of Reference given to this Commission will enable its members to consider not only the regulatory environment pertaining to the design, construction, and maintenance of buildings; but also the public policy environment that will enable improvements to both existing and future buildings over time.

48. Ingham and Griffith in their Report acknowledged the significant financial cost of compliance with seismic strengthening of New Zealand's building stock. This issue has also been outlined in detail by other submitters.

## **CONCLUSION**

49. Property Council has come to the Commission seeking to outline a series of recommendations that would enable property owners and territorial authorities to progress works necessary to evaluate (and enhance) the performance of buildings in New Zealand. This process should start with UMB. At the same time, the taxation obstacles identified in this statement of evidence need to be addressed.

50. It will not be possible to address changes to the Act and the Code without consideration about how changes will be delivered and enforced. The Commission provides a unique opportunity for recommendations to be codified so as to inform the Government's decision-making.

51. Property Council's forward advocacy programme will be shaped to respond not only to changes to the Act and the Code, but also other matters that affect the ability of property owners to fund works that enhance the performance of their buildings for the betterment of the New Zealand public.

52. Property Council thanks for the Commission for the opportunity to appear at this hearing.