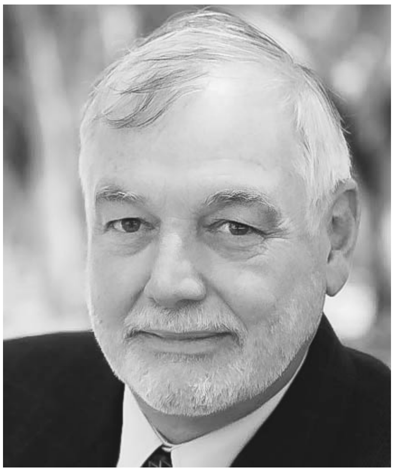
Gateway | Node in the Network | Mish-mash

How to Create and Capture Public Value: Current Debates in North Sydney

Message from Academics and Scholars:

Jeremy Dawkins



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The decision by the NSW Government to construct a Metro line from Rouse Hill in the north west of the Sydney region to Bankstown in the south west has raised many critical issues for regional planning, urban design and the funding of infrastructure.

Canterbury, on the Bankstown line, has been the focus of vigorous debates about dramatic increases in urban density and the validity of funding the Metro through a form of 'value capture' – a question explored in one of the studio projects presented in this Yearbook.

At another critical node on the network, the North Sydney city centre has become a laboratory for urban development and design, as battles are fought over the value and impacts of development.

This is happening, in part, because the North Sydney city centre is a 'pretty appalling CBD'. It 'hasn't had anything remotely like the level of planning and care and attention over the decades that it should have had' (Jeremy Bingham in Park 2001, p.15).

Nevertheless, the North Sydney city centre grew in the final decades of the last century to be the fifth largest CBD in Australia after Sydney, Melbourne, Brisbane and Perth. While it has not kept pace with other cities, it is now catching up. This is the middle of a decade that will see well over 200,000 m2 of high-quality office space added to the city centre. Within a few years, North Sydney, Parramatta and Macquarie Park-North Ryde will each have well over one million square metres of office floor space (by then the Sydney CBD will have between six and seven million square metres of office floor space).

It is widely agreed that these city centres are growing at the expense of suburban business parks, office campuses and other distributed locations, because organisations are competing for knowledge workers who prefer to work where the action is (or at least where the coffee shops and bars are) in a lively urban centre with good public transport. One could say that for these workers, concentration (even congestion) – of tall buildings, people and activity – is a positive externality. This externality has a real monetary value, even if it is hard to quantify. Employers have to increase salaries or add other benefits to attract workers to less interesting locations.

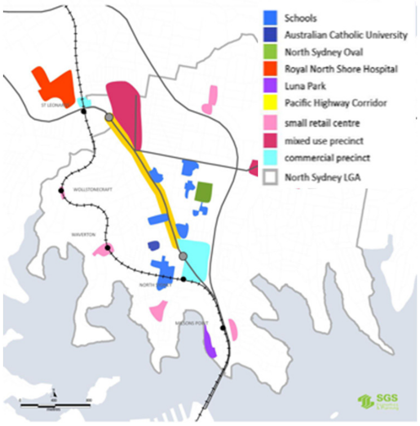

Figure 1: North Sydney and environs *(SGS 2016,P8)*

The attractiveness of North Sydney as a place to work is largely due to its proximity to the real centre of the action: Sydney CBD. Most who work in the North Sydney city centre live on the North Shore (SGS 2016), so their journey to work takes them closer to the Sydney CBD. There is little else to attract them. The judgement given at the beginning of this article, that the North Sydney centre is 'appalling' and that it has not received 'the level of planning and care and attention over the decades that it should have had' was made in 2000 by Jeremy Bingham, lawyer, property development consultant and a former Lord Mayor of the City of Sydney. He had more to say about the North Sydney city centre.

> *Nobody has ever cared much about the North Sydney CBD and it's always been a very deficient CBD in terms of public amenities and open space, public facilities, out-of-hours activities… It has no heart. It has no central point. It has no civic spaces. It has no style. It's a mish-mash (Jeremy Bingham in Park 2001, p.15).*

A 2016 study found that the weaknesses of the North Sydney city centre included 'lack of higher order retailing, limited entertainment options, poor pedestrian amenity and lack of night time economy' (SGS 2016, p.27). In short, it might be a 'Central Business District' but it is not a city centre. As described by the Committee for North Sydney, it is an 'office park with through traffic' (Committee for North Sydney 2018).

Urban change and 'value capture'

Claiming that they can give the city centre a heart and bring public life to the streets, the North Sydney Council is promoting the redevelopment of a peripheral site within the Ward Street block in the northern sector of the CBD. Sydney Metro, on the other hand, claims that a massive commercial tower built over a new underground Metro station on a key central site will 'transform' the city centre, shaping North Sydney's future and 'adding to the vibrancy of the area'. The third voice in this debate is that of the Committee for North Sydney, which aims to 'facilitate public and expert contributions to the progressive improvement of North Sydney, through visionary strategic planning, good public policy and imaginative urban design' (Committee for North Sydney 2019).

These three entities have different understandings of 'value capture'. Value capture is a mechanism in urban management that planners have been advocating for two or three decades, with not much take-up by governments in Australia.

The concept of value capture is based on a simple fact that has shaped land use and land management from antiquity, and has driven the emergence of cities, even though it is a fact that is extraordinarily difficult for most people to hold onto – perhaps because an internalisation of this fact requires a dynamic spatial imagination. Any activity (including doing nothing) on every piece of land has impacts on each piece of land in the vicinity. These impacts are experienced as positive and negative effects, which in turn affect the value of land for different purposes, and thus increase or decrease its market price. An investment that strengthens an urban area in some way – for instance, bringing more people to the area, increasing local services, enlivening public life, increasing accessibility, creating an image – will generate positive impacts for most if not all pieces of land nearby, the geographic extent of the impact being a function of the scale and nature of the investment.

These numberless impacts, from all land parcels to all land parcels, drives the urban property market. A creative and effective developer sees the world as a turbulent sea of positive and negative forces on property values, but it seems that most participants in urban development and management have a flatter, more static, less spatial sense of the city and allow their plans, ideas and accounting to be confined within the boundaries of their site. Unfortunately, this describes the aspatial mindset of most economists and certainly of the NSW Treasury officials who have the most influence over executive government in the State of NSW.

Under strong private property rights, the increases in the market prices of affected land parcels belong to the land owners. They all benefit from investments by others, without making any contribution at all. Of course, when the impacts are negative, land owners have to accept a loss in value without receiving any compensation. To own urban land is to participate in a lottery, a game of luck, in which the value of the asset goes up and down according to external factors over which the owner has no control. This is why these impacts are called 'externalities'. All societies, from prehistory, have regulated land use impacts between neighbours, and have introduced sufficient certainty into urban development to enable an urban property market to function, but none has removed the basic elements of the property lottery in which gains from externalities are retained and losses are uncompensated.

Incentives to invest in major urban projects are influenced by the distribution of positive impacts that raise property values, and the extent to which the increases in value can be retained, recovered or captured by the investor, and thus internalised. Where a developer has a large site, investing in public facilities and high-quality public space will raise the sale price of all land parcels. Enlightened outlays may increase the degree of value capture and the profitability of the project. When governments demand such qualities and facilities through planning instruments, they are often reinforcing what is already in the developer's interest.

A similar form of value capture operated when railways and tram services were private investments. The investor first bought land along the route, then built the infrastructure to make the land attractive, and invariably made their biggest (or only) returns from land, not from operating a transport service. To facilitate this process as railroads were built across the US by the 'robber barons', governments enabled land to be compulsorily taken by the investor, who thereby owned the increase in land value due to the railroad.

Public investments in infrastructure and other urban improvements have used these kinds of mechanisms only intermittently, until recently relying on central tax revenues for funding. For most people owning urban land, paying taxes is largely a lottery. There is seldom a direct connection between taxes paid and benefits derived. Taxes are consolidated into a single fund and spent according to a government's priorities (of course influenced by their constituencies). Typically, the positive externalities from these investments will be distributed unevenly, with some taxpayers funding windfall gains for others.

In the provision of infrastructure, value capture is a mechanism to recover some of these windfall gains, by attempting to match increases in land values on the one hand, and some kind of impost on the other.

Suddenly it is a term that the NSW Government and North Sydney Council have embraced. Unfortunately, the kind of 'value capture' they refer to is a minimal version of the real thing. This will become clear from an examination of the current proposals and policies of the North Sydney Council and Sydney Metro.

Effective and ineffective 'value capture'

Example 1: The Ward Street Precinct master plan

Figure 2: Pedestrain flows in North Sydney

(Source: Mecone 2018, p.24)

In Figure 2, below, Ward Street is the cul de sac at the top of the map, between Miller Street and Walker Street. Its only significance is that the council owns two sites at the end of Ward Street. The sites are used for multi-storey car parks, operated by a tenant, whose lease ends in 2020.

The Council could use these two sites to benefit the city centre in many ways, by selling them to acquire land (or property rights) in a better location, for instance, or by transferring the development entitlements to a more valuable location. Instead the Council appears to have decided to leverage this land exactly where it is, even though the block is somewhat peripheral to the centre of the city, as clearly shown by the pedestrian flows (Figure 2). The block has thus been given a higher significance, reflected in an optimistic description as a 'precinct'. It is also called upon to be the vehicle to transform the city centre, through the implementation of a master plan to deliver a public space of about 500 m2 and a branch of the city library. The consultants on the project advise that the Council:

> *Will be able to deliver the proposed community facilities and public open space through a variety of mechanisms including land sales, planning agreements and value capture (Hassell 2018, p 100).*

It turns out, however, that in this case 'value capture' is achieved by granting a participating land owner a large increase in development potential in return for a proportion of the resulting increase in land value, referred to as the uplift, being contributed by the owner towards the costs of the public components. The consultants illustrate the proposal in the following manner.

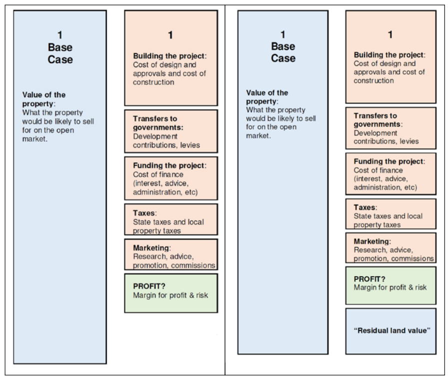

Figure 3 (left) & Figure 4 (right): Value components.

(Redrawn from Hassell 2018, p100)

In Figure 3, the blue bar is the market value of the building, or the completed project. With good luck and good management, there is an amount of profit, after all the usual outlays. The difference between the two bars is the land value, as shown in Figure 4. It's called 'residual', because (in this approach) it is the amount that remains when the other amounts are accounted for.

The consultants then consider the amount of 'uplift' that will be needed to fund the public components of the Ward Street precinct master plan.

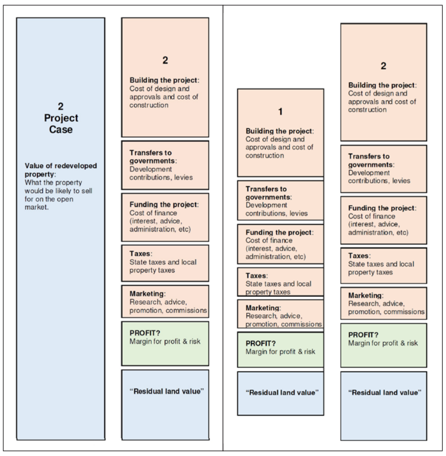

Figure 5 (left) & Figure 6 (right): Value components.
(Redrawn from Hassell 2018, p100)

Figure 5 shows a much bigger project. In the case of the Ward Street precinct master plan, the consultant is contemplating an office tower of up to 57 storeys!

The costs are all higher, the final value is higher, and the residual land value is increased.

Figure 6 compares the various amounts, hypothetically. Again with good luck and good management, the land value has increased significantly.

It is this increase that can be attributed to the project, and allows the council to achieve some measure of 'value capture'.

There are some serious problems with this approach, or at least with applying the term 'value capture' to the scheme.

- Fundamentally, the scheme is misplaced, in that the council should be considering the whole city centre, not just the unimpressive block where it owns land, and employing every mechanism available to it – levies, charges, partnerships, agreements, swaps, transfers, etc – to trigger and sustain a transformation in the quality of public spaces and public life in the city centre.
- Focusing, however, on the Ward Street proposal, it is a perfect example of the condition described above in which, in the absence of a 'dynamic spatial imagination', plans, ideas and accounting are confined within the boundaries of a site.
- The impacts, to and from all buildings in the block and far beyond, are significant, and cannot be ignored in this way. To give two examples: (1) the 'proposed community facilities and public open space' envisaged in the scheme will themselves generate positive externalities such that all land values in the area will increase as a result; (2) equally, the measures used to raise capital – massively larger buildings built up the hill and to the north of the area with already the highest pedestrian flows – will impose significant shadows and winds on the area and thus will reduce both amenity and land values to some degree.
- In other words, the 'uplift' and its opposite (downdrop?) arising from the positive and negative impacts of investment in dense city centres are many, varied and geographically extensive. Any attempt to recover the unearned property value increases that neighbours receive – that is, to capture some of this value – requires a much more sophisticated analysis.
- Trying to account for these and other positive and negative impacts must be an essential element in assessing the merit of the Ward Street proposal, and suggesting there will be a narrow form of 'value capture' without considering these impacts could be highly misleading.
- Finally, the Ward Street proposal demonstrates the enormous incentives that are required to encourage an owner to demolish a building and replace it with something bigger: the margins for profit and increased land value are only two components among many, and they need to be significant, even excessive, to offset the obvious risks in committing very large fixed capital sums into new projects.

Example 2: Sydney Metro's over station development

The simplistic view of value capture confined to one site, as represented by the Ward Street proposal, is exactly the approach being taken by Sydney Metro.

Sydney Metro compulsorily acquired four sites on Miller Street at or near Berry Street, amounting to 4800 sqm, for construction of the underground Metro station serving North Sydney. There is an important item of Australian urban planning history involved in this acquisition. One of the four sites was occupied by Tower Square at 155 Miller Street. It was a two-storey complex of small businesses of the kind that enrich a city centre - in a modest building of courtyards with balconies and stairs in a vaguely Spanish style - operating within favourable economic circumstances since the development rights had been transferred to 65 Berry Street in the 1980s to enable a larger office building to be built there. In other words, the Tower Square site was undercapitalised, which enabled many modest businesses to operate to the benefit of the city centre, in a pleasant 'people place' with a polite built form maximising patterns of sunlight and shade.

Purchase of the strata titles and compensation of the owners and tenants of the Tower Square site might have cost Sydney Metro $50-60 million. The site has now been sold on by Sydney Metro for significantly more than that (maybe double the cost of acquisition), since past planning commitments have been administratively swept aside and the Floor Space Ratio has been effectively increased from 1 to 12.5. The difference is wrongly claimed to be value capture. A better description would be site exploitation.

Two of the other three properties on the amalgamated 4800 sqm site were modern multi-storey office buildings, requiring significant purchase prices, compensation to owners and tenants, and costly demolitions.

To meet their business plan imposed by NSW Treasury, the NSW entity Sydney Metro has been given planning approval by the NSW Department of Planning for the maximum building envelope on the site - 60,000 sqm and 42 storeys high - constrained only by avoiding significant shadows on Brett Whitely Place, Greenwood Plaza and nearby dwelling units.

Sydney Metro announced on 21 December 2018 that the site had been sold to a developer for $200 million. This was claimed to be an exercise in value capture, helping to off-set the $19 billion cost of the Metro project. In fact, it appears to be the market value of this large site in a critical location in the North Sydney city centre. An element in the contract requires the developer to pay more if the valuation of the site increases significantly once the Metro is operational. This reflects an obvious truth: the site is being sold at less than the value it will have once the significant positive externalities from the Metro are realised.

This is actually a property play by a new kind of entity that enjoys the prerogatives of a government agency with property-resumption powers while exercising the 'commercial in confidence' protections of a private business. Sydney Metro is maximising the return on the compulsorily acquired site, using the State Significant Development process to gain approval for a private office tower.

While claiming to be capturing value, Sydney Metro is actually imposing significant negative effects on the rest of the city centre, (1) through the demolition of Tower Square and the expulsion of a valuable cluster of businesses; (2) by imposing negative environmental effects that will arise from a commercial tower that will be the largest and tallest in North Sydney: and (3) by refusing to allow any of this large site to be used either as a public place or for civic activities. This feels more like value destruction than value capture.

Example 3: Possible alternatives

'Value capture' is no more than a debating trick – like 'clean coal' and 'vibrant centre' – in the absence of two essential elements.

- Attempts to implement a policy of value capture must be based on an understanding of the pervasive impacts of every urban investment, and how that investment gener-ates what was described above as a 'sea of positive and negative forces on property values'. If the policy is not informed by a 'dynamic spatial imagination' it cannot begin to assess what values can and should be captured.
- The second precondition for implementing a policy of value capture is that significant unearned increases in property values are enjoyed by identifiable property owners as the consequence of the large and positive externalities generated by a specific in-vestment.

Interestingly, Canterbury and North Sydney are very different cases in relation to the second precondition. A new metro station that connects North Sydney to Crows Nest and a new catchment to the north west, as well as connecting to new locations in the Sydney CBD, will clearly have strong positive impacts. The same is not true of the Metro in Canterbury, since a rail service, fully integrated into Sydney's regional rail system, is being replaced by a single, smaller (if more frequent) Metro line. At peak times, passengers may be able to stand in a Metro car every four minutes rather than sit in a train every seven-and-a-half minutes. What value is there to capture in that?

In the North Sydney case, where the effects on property values can be assessed and quantified, it would be possible to recover some of the 'uplift' directly attributable to the new Metro station through a business district levy of the kind widely used in the US, or the type of charges being used by the high speed rail authority in the UK, or an increment on land tax and/or local rates, or a betterment charge on land sales or redevelopment, or as many other mechanisms as imaginative policy makers can come up with.

A real understanding of value capture would lead to a policy of maximising the increase in property values caused by the new Metro station, and thus the amount of the investment recovered. For example, using the compulsorily acquired Metro site in North Sydney to reproduce some of the excellent 'people' qualities of Tower Square, to add a central public space as a heart for North Sydney on the Miller Street axis (on what would be the only level, sheltered, sunny site in the city centre) and to include around that heart some spaces for civic and civil-society functions would have begun the transformation of the CBD into a city centre, and generated meaningful and appropriate increases in (taxable) property values.

In other words, if a real value capture policy were being implemented, the incentives would be very different. It is characteristic of the curious urban dynamic in Sydney that NSW Treasury should require Sydney Metro to ignore the real mechanisms for value capture, and instead exploit their North Sydney site through property deals, while imposing significant negative impacts on the entire city centre and actually supressing the 'uplift' that should accompany their investment.

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