Valuing Winstone Pulp's Karioi forest

IN THE MATTER OF	A Crown Forestry Licence ("CFL") dated 30 November 1990 between the Crown and Winstone Pulp International Limited
AND	
IN THE MATTER OF	an Arbitration pursuant to Clause 4:4:6 of the CFL for determination of the Land Value as at 30 November 1996
BETWEEN	WINSTONE PULP INTERNATIONAL LIMITED a duly incorporated company having its registered office at Auckland and carrying on business as a forestry company ("WPI")
AND	HER MAJESTY THE QUEEN in right of New Zealand acting by the Minister for State Owned Enterprise and the Minster of Finance pursuant to Section 14 of The Crown Forest Assets Act 1989 ("Crown")
Supplementary Hearing	August 27, 2000
Counsel	Mr MN Dunning for Licensee Mr M Parker for Licensor
Date of Award	October 27, 2000

Additional award of sole arbitrator

Winstone Pulp International Limited (WPI) and Her Majesty the Queen ("Crown") are the parties to a Crown Forest Licence ("CFL") dated 30 November 1990. In terms of that licence the annual rent was subject to review as at November 20, 1996.

As the parties were unable to agree on land value, I was appointed as sole arbitrator and delivered my award on February 4, 1999. After consideration of the evidence I determined a land value as at November 30, 1996 of $8,100,000.

WPI appealed my decision on the basis that I had made errors of law in my award. The appellants asserted that:

- The principles established under the Valuation of Land Act 1951 to assess the value of "land and land value" were not relevant to an assessment of those same factors under the Crown Forest licences; and
- That the Arbitrator erred in not taking into account the pre-plant costs and fertility difference in valuing the land at Karioi.

In a High Court decision dated April 27, 2000 Robertson, J determined there was no error in law on the first issue. However, on the second issue he stated: "I am satisfied that the Umpire by valuing the land as if it were pastoral land to be used for forestry purposes made an error of law. Under the terms of the Licence he was to value the land as it actually was. Depending on the factual situation this may or may not require an adjustment to be made for pre-plant costs, when using the put and take method.

As he made no findings as to what adjustment, if any, should be made the issue must be remitted back to the Arbitrator for his decision on that point."

At a rehearing on August 27, 2000 I received submissions in respect of the pre-plant cost issue from Mr MN Dunning on behalf of WPI and Mr MT Parker on behalf of the Crown.

WPI's position

Mr Dunning summarised the legal position in respect of my decision and the decisions in Tahorakuri as endorsed by Robertson J. Mr Dunning confirmed

that the courts have agreed there is a land owning entity and a forest owning entity and then emphasised the High Court decision which confirmed the land is to be valued as it actually was although recognising that the trees themselves are not included in the value of the land.

Mr Dunning also outlined the evidence presented at the original hearing from WPI, and in particular the briefs of evidence presented by Messrs Wood, McKinley and Reynolds. He then commented on the Crown's evidence presented at the original hearing and concluded that my award should support a deduction of $125/ha over the whole forest and result in a new land value of $6,923,000.

Crown's position

Mr Parker's submission was that in view of Richardson J's decision I should consider his comments and decide to what extent they are relevant in deciding whether as an issue of fact any adjustment to value should be made for pre-plant cost differences between Karioi and the pastoral sales evidence. He emphasised the need to recognise that the purpose of the exercise is to assess the price a purchaser would pay for land subject to the CFL and used for forestry purposes.

He then dealt with pre-plant cost adjustments, identified the differences between the Tahorakuri and Eyrewell decisions and submitted that a prudent purchaser would not take into account the pre-plant cost differences between forestry land and pastoral land. He submitted however, if they did they would use an NPV approach and a post tax approach should be used in completing the calculations.

Pre-plant costs at Karioi

The land at Karioi has been used for forestry over a number of years. It is all planted in forest and on inspection and based on the evidence at the hearing it is clearly evident there are costs to the licensee in clearing away debris and preparing the land for replanting after harvesting. Those issues were not in dispute.

The pre-plant costs are essentially divided into two principal operations. The first is the clearing away of the slash/debris of the previous crop, and the second the cultivation and mounding of the land to plant the new seedlings above the coldest ground frost levels.

The issue before me at both hearings was to consider to what extent the pre-plant costs that were incurred at Karioi would impact on the price a purchaser would pay for the land.

My conclusion

Richardson J emphasised that when considering land value I was to assess the land as it actually was at the commencement of the licence. He stated: " Depending on the factual situation this may or may not require an adjustment for pre-plant costs, when using the put and take method."

The Tahorakuri decision proceeded to the Court of Appeal which directed the High Court to readdress the quantum of pre-plant costs in that case. In the High Court's second decision and as identified in my award the Court noted that any adjustment for pre-plant costs will vary from forest block to forest block.

They stated: "Where there are clear cost savings the adjustment from actual pastoral land state to assumed forest state may be significant. Where the distinction between the two states does not result in demonstrably pre-plant or weed control cost savings then the adjustment may be minimal or even non existent. In our view the evidence accepted in this case should not lead to the conclusion that all pastoral land sales used for forest land comparison should be adjusted in the same manner and a case-by-case consideration of each of the factors affecting land value is required.

In the Eyrewell Decision, which is on land of similar contour to the subject, it was held that no pre-plant cost adjustment was necessary. The evidence before that Court confirmed that it was cheaper to plant in cut over forest land than in pastoral land.

That there are issues of pre-plant costs applicable in Karioi is not in dispute and the evidence was well presented. The licensee does incur costs between harvest and replanting. There was considerable debate as to whether those costs were tax deductible or needed to be capitalised. However, those issues would only be significant if I were satisfied that the market in establishing a land value at Karioi would make an additional deduction for pre-plant costs when comparing with the sales evidence used to establish value.

Identified on page 15 of my award is the value I adopted as a "starting point" after consideration of the evidence and inspection of the sales. That value was $9,046,500. I then considered the adjustments required, if any, having regard to the evidence presented at the hearing.

That starting value was established after careful consideration of the market evidence. As confirmed in the final High Court Decision on Tahorakuri when applying the sales evidence to the land being valued there must be a case-by-case consideration of each of the factors affecting land value.

The sales evidence considered was principally pastoral land purchased by foresters for conversion to forestry. This differed from the evidence presented in the Tahorakuri case where much of the evidence was on pastoral to pastoral sales.

The principal purchaser through the King Country was Carter Holt Harvey but other purchasers included private investors and syndicates. There was not evidence presented to suggest that any of these

purchasers of land for forestry purposes were other than well informed.

It is my view that when adjusting sales evidence and applying that to the property being assessed care must be taken not to allow for adjustments which may already have been taken into account in the sales. Mr Reynolds, acting on behalf of the licensee confirmed that when making his adjustment for pre-plant costs he was relying on the decisions in Tahorakuri. The final conclusion in that case however, emphasised the need to consider the facts in each case. Just because pre-plant costs were accepted in Tahorakuri it would not necessarily follow that a deduction for pre-plant costs would be applicable in the subject case.

I raised this issue at the second hearing by asking the parties whether it was possible that when purchasers acquire pastoral land for conversion to forestry that any deduction for pre-plant costs was already factored into the price. It was Mr Parker's view that purchasers of pastoral land for conversion to forest take into account all forestry costs when determining price. Mr Dunning replied that there was no evidence that purchasers of pastoral land for forestry purposes did take pre-plant costs into account when establishing price.

In deciding to allow for pre-plant costs Mr Reynolds not only relied on the legal decisions of Tahorakuri but also on the evidence presented by the licensee of actual pre-plant costs in this forest. There was no evidence presented to me however, that those same costs or other similar pre-plant costs would not apply to the sales evidence used as a basis for assessment. The representatives of WPI confirm they did take pre-plant costs into account when determining what to pay for land. As all were well informed it would follow that the purchasers of the various blocks used a basis in the assessment also took those factors into account. Unless it can be clearly shown that the pre-plant cost issue was not taken into account in the sales evidence, it is my view that when making an additional deduction for pre-plant costs one may well be double counting.

The pre-plant costs at Karioi were divided into two sectors. One was the mounding of the land to plant slightly above the original ground level, which is a feature of the land in this location and should be taken into account when considering the use of this locality for forestry purposes. I am satisfied that factor has been allowed for in the adjustments already made for location, contour and production when arriving at the starting value of just over $9,000,000.

The second issue of clearing slash and debris, which is the other factor of pre-plant cost, could occur in all forestry situations. To make an additional adjustment for that purpose I would have required evidence to clearly establish that those same or similar costs would not be incurred on the sales evidence used as a basis for this assessment. This exercise was not done as confirmed by Mr Reynolds in his answers to Mr Parker's questions at the hearing.

There was no disagreement between the parties that the purchasers of the sales used as a basis for this assessment were other than well informed foresters who were purchasing pastoral land for conversion to forest. In absence of any clear evidence to the contrary one can only assume that those purchasers took all factors into account when acquiring land for conversion to forestry. If pre-plant costs were relevant and not considered, then those purchases would immediately suffer a decline in value once they planted the land in trees. There was no evidence that situation applied in any of the sales all of which were negotiated freely on the open market on a willing seller/willing buyer basis.

Award

After consideration of the evidence presented at the original and second hearing, I am of the view that in this case the facts as presented to me would not justify an additional deduction for pre-planting costs. I therefore confirm the land value for the karioi forest as at November 1996 at $8,100,000 (eight million one hundred thousand dollars).

K G Stevenson
Arbitrator

Note: This is the second award made in respect of this case, which relates to Crown Forest Licenses. The first award was included in The Valuer's Journal, July edition 1999.