

New Zealand Valuers' Journal - November 1998

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NEW ZEALAND VALUERS' JOURNAL

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3. Comment	Author; Title; Publication

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Editorial

Preparation of roll valuations

After September 2000 Territorial Authorities (TA's) will no longer be legally bound to receive their Rating Roll Valuations from Quotable Value. Already 13 of the 74 TA's with two more pending, have decided to make this work contestable. Section 61 of the Rating Valuations Act 1998 makes provision for the changes to be on a gradual basis.

The new environment has been in place since 1 July 1998. In keeping with the process of change every aspect has not been straightforward. Dividing the old Valuation Department into Quotable Value New Zealand and the Office of Valuer General required not only extensive restructuring but also the adoption of a new outlook, philosophy and practice.

Quotable Value was born from a monopoly with no market price against which it could measure the cost of valuation roll services provided to local government. Investment in technology and fewer staff have streamlined the organisation at each of its offices. When Invercargill City Council and Tararua District Council tendered for the valuation roll services they both found in favour of private

valuation firms. In Marlborough the District Council stayed with Quotable Value. Clearly there has been a learning curve.

Within the last few months a further ten Councils have been gazetted as transferred into the contestable environment. These are Ashburton District Council, Nelson City Council, Rangitikei District Council, Selwyn District Council, South Waikato District Council, Thames Coromandel District Council, Tauranga City Council, Waikato District Council, Matamata Piako District Council and Hamilton City Council. Two more councils are imminent but have yet to be gazetted.

For the TA the opportunity to go contestable is in keeping with the contracting out of other services. Savings must clearly be expected but standards need to be maintained. There have been new developments here with the clustering of TA's calling tenders for the services of property valuation. The Waikato is a particular example. Here, several councils are negotiating together for the letting of a contract. Some councils have found compliance problems with the legislation mainly in terms of the revaluation date

of their district valuation roll. These need to be brought into line so that the new systems are in place by September 2000.

Part and parcel of the whole restructuring process has been the devolution of the National Property Data Base into some 74 districts so that they can be devolved to the TA which then takes over responsibility for its area. The question of cost saving here is more debatable; they may set up their own information system or they may lease the services from a dedicated provider or from valuation firms willing to invest in the technology. For individual valuers access to the service may cost more or less this is currently uncertain. Quotable Value has a facilities management scheme and other valuation firms will have to compete with this. Because the OVG sets the standards and the rules more consistency in the results of valuation maybe expected; it will have an ongoing monitoring/auditing function. In terms of quality there are therefore likely to be benefits.

Then there is the question of whether rates that are set on property values, a tradition since the 19th Century, is the

way of the future. Some TA's have already introduced fees and user charges moving away from the property value rates as a major source of revenue to fund services. A discussion document released recently by the Minister for Local Government does not mention a wholesale move from basing rates on property value but it does raise the prospect that residential rates in future could be split. In this case part would be based on value and the rest would be a flat charge on each property.

The introduction of contestability into the rating roll area has clearly had ramifications beyond those that were expected. Now it will be

of interest to see if the Crown also considers whether or not it is necessary to compulsorily maintain capital values as a basis for rating or whether they rate purely on land values.

Note: Because of the late release of this Journal owing to repetitive technical problems this editorial is written as of April 1998. On behalf of the New Zealand Institute of Valuers the editor apologises to subscribers for the production delays.

With the restructuring of Valuation New Zealand on 1 July 1998 the administration of the Valuers Registration Board now functions as part of the new Office of the Valuer General in Land Information, NZ.

All of the Registrar's contact details have changed:

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Resource Management Act: Is there a need For more reform?

Matthew McClelland,
Adam Pope and
Jo Elliott

The recent publication of the Ministry for the Environment's *Proposals for Amendment to the Resource Management Act* (November 1998) details proposed amendments to the Resource Management Act 1991 ("the RMA") and suggests ways in which the Act could be refined. Essentially, the objectives of the proposed amendments are to reduce duplication, uncertainty and costs of compliance, and to improve the practice and procedures of the Act.

The enactment in 1991 of the RMA was intended to create a comprehensive framework for resource management in New Zealand. Underlying the legislative reforms in 1991 was the desire to promote the sustainable management of natural and physical resources on land, air and water within the one comprehensive statutory regime.

Perhaps inevitably, from the date of its inception the RMA has attracted intense debate and criticism from almost the complete spectrum of people and organisations with an interest in natural resources or environmental management. There has been

much debate over the last seven years as to whether or not the RMA achieves its sole purpose of promoting sustainable management and in respect of the perceived difficulties and inequities resulting from the implementation of the Act. More recently, there has been repeated criticism in some sections of the media about the costs of compliance for business, the lengthy delays that can be incurred in obtaining resource consents and the issues surrounding consultation and development of the plans and policies required under the RMA at district, regional and national level.

While the criticisms made in respect of the RMA originate from a wide variety of interested stakeholders and there would be few people who would deny that there are very real problems with some parts of the current resource management process, the question has been asked by some commentators as to whether the source of those difficulties lies within the provisions of the RMA itself, or, whether the implementation of the RMA by Government, both central and

local, and stakeholders is the primary reason for the difficulties that many interested parties consider to exist at the current time.

As one author has noted, *"The RMA will deliver on the high expectations of the purpose and principals [contained in the Act] only if all those using the legislation perform well"* (Lineham [1998] BRM Gazette ppl-3). In considering the implementation of the RMA it is therefore important to recognise that while the RMA puts in place a regime for preparing district, regional and national plans and policies together with processes for obtaining resource consent for land, air and water use, the primary responsibility for implementing the provisions of the Act lies in the hands of government and, in particular, local territorial authorities.

The consequence of this is that while the RMA provides the framework within which provision is made as to how best to balance the various aspects of resource use, the decision making process takes place at a more local level, seemingly often in isolation from decisions being made by other territorial authorities. As Simon Upton observed last year:

"This places real power and responsibility in the hands of councillors. The policies that govern air and water pollution, amenity and landscape values and all the mirror rules needed to keep neighbours from going to war with one another are in their hands." (Herald, 5 August 1997)

Legislative Amendments to the RMA

Since the RMA first came into effect there have been five separate Acts passed amending different portions of it with the intention of improving both the resource consent and plan/policy development processes set out in the Act.

In addition to the amendments made to the RMA, a relatively large number of regulations, currently 16, have been passed to make it workable and, over the last 7 years, the Environment Court (formerly the Planning Tribunal), the District Court, the High Court and the Court of Appeal have, between them, heard several thousand proceedings under the RMA, establishing a relevant and comprehensive body of caselaw dealing with interpretation and policy matters under the Act. Indeed, as it was noted last year in the Butterworths Resource Management Bulletin:

"It is hard to imagine that any law reform process and subsequent implementation of legislation could have been more extensive, inclusive or rigorous. Indeed there is probably not a lot wrong with the law itself. Rather the problems lie in the varying understandings of the purposes and functions contained in the legislation, the varying applications of these principles in policies, plans and consent decision making, and the lack of

communication between the various levels of central and local government." (David Grinlinton [1997]2BRNB49at 50)

The Proposed Amendments to the RMA

The current proposals by the Ministry for the Environment represent another attempt to reform different portions of the RMA with the intention of improving the resource consent and plan/policy development processes contained in the Act.

The Ministry's report recognises that concern has been expressed that the functions of district and regional councils overlap, causing confusion and imposing unnecessary costs on resource users. A number of the amendments are proposed to alter the functions of regional and district councils to eliminate duplication. These include the mandatory transfer of the administration of any rules in a plan to district councils, and the re-definition of the policy making responsibilities of district and regional councils. These proposals do go some way towards addressing the issue of performance under the Act by territorial authorities.

Other amendments proposed are aimed at making national policy statements a more attractive way for central government to guide local authorities and influence processes and decisions made under the Act. National Policy

Statements have not been used partly because of the perceived lengthy and uncertain process involved in their promulgation.

Perhaps the key change proposed to the scope of the RMA is a revised definition of "environment". The current definition is thought to be concerned with an unlimited range of adverse effects. The Government proposes to change the definition to limit its range to health, safety, amenity and cultural values of people and communities. Social and economic matters beyond this more precise list are to be removed.

Other proposed amendments relate to resource consents and are designed to reduce costs and to improve the process of making an application and notifying and considering applications.

It is proposed to introduce contestability into resource consent processing such that an applicant will be able to use private sector companies instead of council staff to process their applications. One implication of introducing contestability into the consent process is that private consent processors will not notify applications which should be notified because of pressure from the applicant. No provision has been included in the proposals to explicitly address this issue.

It is also proposed to put in place a new procedure whereby consent applications could be directly referred to the Environment Court, the primary rationale for the proposal being to reduce the cost of hearings in

cases where appeals are inevitable. Issues as to the question of processing times would obviously need to be considered if this proposal is adopted. Amendments to the Act are also proposed to ensure that local authorities are more accountable in terms of processing times.

Under the existing system, resource consent applications can potentially be the subject of two hearings on the facts. It is believed that this approach creates significant opportunity for any party seeking to frustrate a resource consent applicant to threaten appeal as a means of deterring the applicant from continuing with their application. For many applicants, two hearings on the facts can be beyond their resources. It is therefore, proposed to reduce the opportunity for this to occur by limiting the rights of appeal on resource consents to points of law only (rather than a *de novo* appeal which requires another hearing on the facts).

It is acknowledged that if the opportunity for a *de novo* appeal at the Environment Court is removed, local authority hearings would come under increased scrutiny. Accordingly, it is proposed that independent commissioners be required for all hearings. This would potentially remove the decision-making from any suggestion of political interference and elected representatives on local authorities would be free to assist constituents in a way they are precluded from doing so if they are the decision makers themselves. Issues as to who would qualify to be a

commissioner, how commissioners would be appointed and by whom remain unresolved.

In respect of subdivisions, it is proposed that subdivision remains in the RMA as it is recognised as being a useful tool for managing the effects of land uses. Amendments are proposed to allow a local authority to minimise subdivision control and focus on simply controlling land uses. It is proposed to amend the Act so that subdivision be permitted unless it is controlled by a rule in the plan.

Improving Processes Under the RMA Some Conclusions

If the undoubted problems with the implementation of the RMA do not lie primarily with the law itself, then the focus of attention must shift primarily to those parties using the legislation and, in particular, to local and central government as the primary decision makers under the RMA. The practical effect of leaving the implementation process for obtaining resource consents for land, air and water use and for preparing plans and policies to territorial authorities has resulted in markedly different approaches being taken by territorial authorities on a wide variety of matters under the RMA, including environmental assessment, the appropriate consideration of Maori interests, protection of cultural heritage, the development of district and regional plans.

Hopefully, the Ministry for the

Environment's current proposals will address the key issues of performance under the RMA by all stakeholder groups and, especially, by territorial authorities. Certainly, they attempt to go some way towards addressing some of the key implementation issues. The authors, however, consider that there remains considerably more that needs to be undertaken, other than further amendments to the Act itself, to encourage the development of consistent approaches to the purpose, principles and functions set out in the RMA by territorial authorities. Much of this could be achieved through the preparation of national policy statements and national environmental standards as envisaged under the RMA since the date of its inception. These would at least give some standardised direction and enforcement on key concepts. Further, more resources should be provided for implementation purposes, particularly to enable the Act's current processes to be effectively monitored.

The authors consider that while there remains scope for improvement to the RMA itself, and while the current proposals attempt to address a number of the issues, many of the criticisms currently being vocalised in the media and elsewhere could be resolved within the existing regime without any further major reform of the legislation. Where there are wide discrepancies between the approaches taken by territorial authorities we consider that it is incumbent on central

government to provide resources, direction and a means of enforcement to ensure that the purpose underlying the RMA is pursued as consistently and expeditiously as possible.

Public submissions on the proposed amendments have been called for and are open until 29 January 1999. The authors encourage everyone to consider the proposed amendments and their potential consequences closely and make submissions accordingly.

Matthew McClelland

About the Authors

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Jo Elliott is a solicitor in the litigation department of Kensington Swan's Wellington office. She is a member of the firm's Resource Management Work Group.

Adam Pope

EEO Policies and Practices for Valuation

Marie Koreman

This is the third in a series of articles by Marie Koreman for the 1998 Journals of the New Zealand Institute of Valuers. Marie, from Equity Works in Auckland, is the Institute's equal employment opportunities (EEO) Consultant.

The first of the three articles examined New Zealand's discrimination law and its effects on the rights and responsibilities of employees and employers. The second article analysed the available statistics on the position of women valuers vis a vis men valuers within the profession. It demonstrated that an increasing number of women in the younger age groups of the profession require valuation employers to examine their employment practices to ensure they are able to attract and retain women equally with men in order to be competitive in the employment market.

This article provides some practical ideas as to policies and practices employers can implement to ensure EEO is provided to all employees.

Because of the demographic forces within the profession, the focus of EEO implementation for valuers is currently to attract and retain the growing number of women who are entering the profession. The benefits of EEO, however, accrue to all valuers, including men and people who may need special assistance in order to be able to offer an equal contribution to the profession, or who require special understanding in order to have their equal contribution recognised.

What is EEO?

EEO means actively identifying and eliminating barriers to ensure:

- All potential employees are considered for their employment of choice.
- All employees are given the opportunity to perform to their maximum ability.
- All employees are given the same recognition for equal contribution.
- All employees are given the same recognition for equal contribution.

EEO offers employers the likelihood that they will:

- Attract the largest possible pool of job applicants from which to select new employees.
- Benefit from top performance of employees whose contribution won't be stymied because of unnecessary barriers.
- Save costs by extending employee loyalty and retention through implementing fair employment practices.
- Comply with discrimination law and the Institute's code of ethics.

In addition, EEO offers employers the possibility that they will:

- Enhance their reputation in the profession and in the community by implementing EEO practices.
- Increase their client base by becoming more accessible to demographically diverse clients such as women, Maori and people from Asian communities.

EEO is NOT about:

- Quotas - there are no percentages set for employers;
- Tokenism - recruiting a women primarily because of her sex;
- Reverse discrimination - it does not replace one form of injustice with another, because it applies the merit principle and sound personnel practices to ensure fairness for all employees.

Myths about EEO

There are several myths that employers are inclined to associate with EEO:

- *EEO policies and practices are not needed for small workplaces.*

This is an important issue to address from the outset when considering the valuation profession, as most employers of valuers are small employers. Small employers are unlikely to require an elaborate EEO programme. Non-discriminatory recruitment, training, work allocation and promotion practices ought to occur in any sized organisation, however. Strategies for managing the balance between work and family are also likely to be necessary, as will be an anti-harassment programme and attention to inclusive behaviour in the work environment.

Regardless of the size of the organisation, all of these things cannot be guaranteed to occur without some formal attention being paid to EEO matters. EEO policies and practices, and some

mechanism for monitoring EEO success are relevant for all valuation employers irrespective of size.

- *Formal EEO is not needed - we have informal EEO*

Many employers believe that because they have an attitude of treating all employees the same irrespective of sex, race, age or other factors, formal implementation of EEO measures is unnecessary.

Not all employers who treat employees the same, however, will be implementing EEO. In fact EEO often requires treating employees differently, and acknowledging their various needs in order to provide them with equal opportunities at work. For example, requiring all employees to attend important staff meetings at 8.00 a.m. twice a week may discriminate against those who find it extremely difficult to arrive at work before 8.45 a.m. because they must drop children at school. An employee who struggled to meet this 8.00 a.m. commitment may well be being treated the same as everyone else in being required to attend meetings at that time, but his or her performance may be impaired through being unable to regularly fulfil this obligation. In a similar way, requiring all employees to provide written reports on a training course they have attended may appear to be treating them all the same but may disadvantage an employee who, for cultural reasons, may prefer to give an oral report.

Part of having formal EEO strategies in place is to open

dialogue on employee's special needs with the employer, needs which employees are unlikely to bring to the attention of an employer who insists on treating everybody the same.

Recruitment

Eliminating discrimination at the recruitment stage is the first step in ensuring EEO within the valuation profession. Being small, most valuation employers will have relatively informal recruitment practices and interview techniques.

Eliminate direct discrimination

The first step in eliminating discrimination in recruitment is EEO awareness of those involved in employee selection. Employers need to recognise any prejudices they may have against potential employees, for example on the basis of sex or race. Such prejudices need to be put aside and selection be based on job-related merit in order for EEO to occur at the recruitment level.

An excellent source of EEO education for valuers is a book written by Gill Gatfield, *Without Prejudice - Women in the Law*, Brookers, Wellington, 1996. An examination of discrimination against women in the New Zealand legal profession, this book provides a useful analysis of sex discrimination in employment that, although focused on the legal profession, can be applied to all New Zealand professions, including valuation. I recommend this book to all professional employers who wish

to eliminate discrimination from their firm of business.

Advertising

Filling vacancies through informal processes such as shoulder-tapping or utilising informal networks of friends, family or employees' families limits the number of potential employees who will get to hear of your vacancy. Existing networks often disadvantage relative newcomers to the profession, such as women and people from minority ethnic backgrounds.

Good EEO practice requires that vacancies be widely advertised. Stating in an advertisement that you are an EEO employer may encourage minority employees to apply. The opportunity to work for an EEO employer may be as big or more of an incentive than other benefits often held out by employers, such as local recreational facilities.

The Human Rights Commission has a publication entitled *Pre-Employment Guidelines* which provides good information about non-discriminatory pre-employment practices and assists compliance with anti-discrimination law.

Interviewing

Failure to standardise interview questions to ensure that each applicant is asked the same question opens up the selection process to unfair discrimination, for example women may be asked about their child care arrangements, but men may not be. This sort of questioning often indicates bias on

behalf of an interviewer. Men and women should be asked exactly the same questions so that all applicants are given the same opportunity to demonstrate their skills and potential.

Work and Family

A great deal of progress has been made in New Zealand towards balancing the needs of work and family. Work/family initiatives are not only ones which contribute to the retention of women valuers with young children, but are initiatives from which most men who are parents can benefit from EEO as well.

Male and female employees with children of all ages can benefit from an employer who is sensitive to the needs of working parents. Employers who address work/family imbalance are likely to reap the benefits in greater employee loyalty and retention, and decreased sick leave, absenteeism, lateness and what is popularly referred to as "family-work spillover", (family-related stress spilling over into the workplace to impair work performance).

Examples of work/family initiatives a small employer can implement include:

Maintaining contact with employees on parental leave through personal visits, telephone calls, sending relevant professional and firm newsletters and inviting employees to staff meetings. Involving employees on leave by these simple means has been demonstrated to have a marked positive effect by

increasing the return rates of employees on parental leave. **Being open to offering staggered return options for employees on parental leave.** Some employees will be more likely to return to work, or to return earlier, if they are offered the option of reduced daily hours, or for example, three-day weeks to help ease their return and establish a new routine incorporating work and child care.

- Research available local child care options, including child care centres, nannies, Bamado's home care and shared care. Provide this information to employees with pre-school children to make the job of arranging care while they work for you easier and less stressful. This may encourage new parents to return to work earlier than planned, and/or reduce absenteeism as employees are enabled to find the child care that best suits their work commitments.
- Do the same regarding school holiday and after school care for older children. Research what is available through local schools, community organisations, churches or councils. Where programmes are not available you may be able to establish shared care networks with the employees of other local employers, or encourage two employees to share many services, thus reducing the amount of leave your own employees require.
- Be open to allowing flexible working hours of staff to facilitate dependent care

responsibilities. A forty-hour working week may not need to be worked by five eight-hour days. Allowing employees to carry out paper-work at home, or to work some ten-hour and some six-hour days may enable them to see more of their children or share the school pick-ups with a partner, while still doing all that is required for the employer.

- Consider job-share with part-time positions so as to be able to employ talented employees who wish to work, but who do not wish to work full-time because of family commitments.
- Be sensitive to the needs of employees to spend time with children before school and on weekends. Where possible, avoid early morning and weekend meetings or training sessions that are likely to create work/family stress for employees with children.
- Be open to negotiating extra leave entitlements for employees with family responsibilities. Employees may be happy to reduce their salary in return for additional leave over school holiday periods.
- Consider assistance with child care costs as a part of remuneration packages for employees with family responsibilities.
- Recognise that some employees may require the same kinds of flexibility to enable them to care for elderly

dependants, such as parents. For example, an employee with an elderly parent at home may benefit from flexible hours allowing them a longer lunch period to check on the elderly person and/or heat their midday meal.

Promotion

To ensure EEO employment practices must be such that all employees have equal access to promotional opportunities. Monitoring promotional trends will give an employer an indication as to whether promotional discrimination is operating. For example, are men and women taking a similar length of time before being promoted to associate status? If not, what could be the reason? Could it be direct discrimination, i.e. a direct decision not to promote someone because of their sex? Or could it be that members of one sex are more likely to be given high fee-earning files or prestigious clients so that their performance appears better than fellow employees of the opposite sex?

Unfair work allocation is a primary factor in unequal promotion of men and women professionals. Are women being offered the same opportunity to do rural valuation as men valuers? If women valuers prefer urban valuation but promotion depends on rural experience, are women valuers informed of the need to do both urban and rural valuation by their employer?

If a woman has had a career break to have a child, is the additional

experience she has gained from motherhood valued when considering her management and organisational expertise and maturity?

It is these sorts of questions employers must ask themselves to ensure they provide equal promotional opportunities to all employees.

Rewards

Being flexible with remuneration and rewards packages can enhance EEO. Providing additional leave or subsidising child care as part of an employee's package may not cost an employer extra money, but may foster the perception of a caring employer and enhance employee loyalty.

If "perks" are offered, make sure all employees get to benefit. For example, not all employees will value free tickets to a rugby match - make sure an alternative is available for employees who have different interests. Some employers adopt a shopping basket approach to employee awards or Christmas presents. You could give employees a choice from a selection of benefits, such as a day's leave, dinner for two, a beauty therapy, book or liquor voucher.

Environment

Consider the physical environment of the firm's office. Is it inclusive of all employees. corridors lined with the photographs of male partners in oak frames are legitimate history, but if not balanced they emphasize

the maleness of the profession and make it difficult for women to feel an equal part of the firm.

Displaying Maori art will acknowledge the culture and being of Maori employees, as well as increasing the approachability of the firm to Maori clients.

Simple things such as these, and allowing employees to display a family photograph or a religious affirmation on their desk make people feel acknowledged and valued for their individuality. They increase employee happiness and cost the employer little or nothing.

Harassment Prevention

Workplace harassment can be defined as unwelcome or offensive verbal, physical, written or visual behaviour that an employee finds detrimental. Workplace harassment may be sexual, or it may occur on the basis of an employee's sex, race, colour, national or ethnic origins, disability, age, religion, political opinion, sexual orientation, marital or family status.

Steps to be taken to prevent workplace harassment are clear, and if maintained over time, provide employers with a defence to complaints of harassment taken to the Human Rights Commission.

Policy

Have a written policy statement that defines harassment and makes it clear that it is totally unacceptable. Include in the policy statement examples of

behaviours that are inconsistent with the policy, e.g. displaying sexual pictures at work, making sexist comments or jokes, or using racially-based nicknames.

Complaints' procedure

Having a written complaints' procedure that makes it clear who to report harassment to and that guarantees harassment complaints will be taken seriously. Most harassment complaints' procedures will encourage resolution of complaints through mediation between the employees concerned, as well as the investigation with potential disciplinary consequences of very serious allegations.

Contact people

Large employers ought to have a network of specially-training harassment contact people who are available to discuss harassment concerns and who can explain the firm's complaints' process. For small employers it will suffice to make it clear which managers/partner employees out to report harassment concerns to without fear of reprisals.

Training and education

Make sure all employees understand the harassment prevention policy through education initiatives. For a large organisation this ought to be through providing training workshops for managers and staff. Consultants are available to provide this sort of training. For a small organisation it may suffice to address the harassment policy in a staff meeting, and support it with the distribution of brochures

and handbooks and the display of workplace posters. Equity Works Ltd can provide such support materials.

Resources

Small employers can access a variety of cost-effective resources to assist them implement EEO. Two principal sources of material are the EEO Trust and the Human Rights Commission.

EEO Trust

The EEO Trust is an organisation funded jointly by private sector employers and government. Its purpose is to promote to New Zealand employers the implementation of EEO principles and EEO best practice in the workplace as a means of improving their effectiveness, efficiency and competitiveness through the successful management of diversity.

The Trust has an EEO referral database, access to which is free through the Trust's information manager. The EEO referral database has listings of over 2000 EEO resources such as books, articles, videos, leaflets, manuals and information about workplace initiatives. A report can be customised to your requirements, and includes a summary of relevant resources, details of from where they may be obtained and the cost, (if any). To request a search of the database, employers can contact the EEO Trust:

E-mail: admin@eeotrust.org.nz
Telephone: (09) 525 3023
Facsimile: (09) 525 7076

The Trust also produces a resource catalogue which details reasonably-priced resources covering the subject areas of general EEO, multi-cultural issues, Maori, work and family, gender, disability, sexual orientation and HIV/Aids. These resources may be ordered directly from the Trust and through its internet site at www.eeotrust.org.nz.

Human Rights Commission

The Human Rights Commission produces free and low-cost publications that explain the application of the Human Rights Act 1993 to employment. Contact details for the Commission are

E-mail: help@hrc.co.nz
Internet site: www.hrc.co.nz
Telephone: (09) 309 0874 or
toll free 0508 505 808
Facsimile: (09) 377 3593;
(04) 4710858; (03) 379 2019

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Marie is qualified in law and human resource management. Director of management constancy Equity Works Ltd., Marie practises in the fields of conflict resolution, harassment prevention and equal employment opportunity measures. Earlier this year she advised on the development of a discrimination and harassment complaints' procedure for the Institute and trained a group of members to act as EEO contact people for the profession.

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Valuation in an emerging Market Economy - *the case of Vietnam*

Lim Lan Yuan

This paper highlights the role of the valuation profession in an emerging market economy, Vietnam, and examines the various valuation needs and issues that arise in such an economy.

It is found that while the Vietnamese economy has made significant progress through its economic reforms launched in 1986, the real estate sector remains small and underdeveloped. Nonetheless, the demands for valuation, particularly in the public sector is substantial.

The issues and problems facing valuers in Vietnam mainly arise from thin market transactions and the complex and numerous legislations governing real estate investment and development. There is also a lack of trained valuers who are well versed with the concepts and workings of a market economy.

The Vietnamese government recognises the important role of valuers and plans are underway to develop the profession. In addition to implementing legislation, the various restrictions imposed on the transfer of land use rights and property as well as on mortgage loan financing and sub-leasing

should be reviewed, and where possible lifted.

1.0 INTRODUCTION

In developed or more mature real estate markets such as those of the US, UK, Australia, New Zealand even those of Singapore and Malaysia, valuation is regarded as a key discipline within the real estate industry. It is recognised as a professional service which is fundamental to the functioning of the real estate market. In these countries, the task of valuation is performed by professionals who are trained and skilled in the field of valuation. These valuers are also often engaged to give advice on real estate investments and finance, real estate planning and development and real estate marketing and management.

In developing or emerging market economies such as Vietnam and Myanmar, the tasks of valuation, however, are likely to be handled in a rather rudimentary manner. This may be attributed in part to the lack of well trained and skilled valuation professionals as well as to the less developed real estate market.

Valuers undertaking valuations in emerging market economies such

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in April of this year.
It won the Founder's Award
for Technical Excellence*

as Vietnam face problems and issues which are often taken for granted in the US, UK and other more developed economies. Political, cultural, social and behavioural patterns and business customs and practices in developing countries are vastly different from those in the developed economies. These may give rise to various unique and salient features of the property market which must be taken into account when valuing properties in these countries. Valuers will generally not undertake valuations in other countries without any knowledge and experience of the local markets. However, with the growth of multi-national companies and the globalisation of real estate, an appreciation of real estate markets and valuation practices in other countries, particularly those which actively seek foreign investments, is desirable. In some instances, valuers may be required by multi-national firms with headquarters in their home countries to give advice on real estate investments in other countries. There is, however, a paucity of information on valuation practice in many countries, particularly those which have only recently opened up their economies. Published works such as "Real Estate Valuation on Global Markets" (Gelbtuch, Mackmin and Milgrim ed. 1997) are few and far between.

The objective of this paper is to highlight the role of the valuation profession in an emerging market economy, specially Vietnam, as well as to examine the various

valuation needs and issues that arise in such an economy. Vietnam, which is the latest member of the Association of South East Asian Economies (ASEAN), is used as a case study in this paper, as its economy is in transition from a centrally-planned economy to a market economy with state management. Various ways to develop the valuation profession in Vietnam are discussed taking into account the specific requirements and characteristics of its real estate market.

This paper comprises 11 sections. This section introduces the paper and provides the objectives of the paper. Section 2 gives an overview of the policy of economic reform first adopted by the Vietnamese Government in 1986. Sections 3, 4 and 5 explain the legal and institutional framework within which the real estate market operates and which impinge on property valuation. Section 6 then briefly describes the state of the property market in Vietnam and highlights some of its salient features. Having provided the background of the real estate market in which valuers have to perform their tasks, the paper then proceeds to examine the country's various valuation needs in section 7. Next the valuation methodologies that are commonly used are discussed. Section 9 then examines the valuation issues that currently confront the government, valuers and property investors alike in Vietnam. Measures that are being planned and could be

implemented to develop the valuation profession in Vietnam are discussed in section 10. Section 11 concludes the paper.

2.0 VIETNAM'S ECONOMIC REFORM

Vietnam, located in the centre of South East Asia and bordered by China, Laos and Cambodia, has a land mass of approximately 331,688 sq.k and a population of some 74 million estimated as at 1994. Its capital, Hanoi, has a population of some 3.5 million, while Ho Chi Minh City (still known as Saigon) has a population of nearly 4 million and is the country's main industrial and commercial centre. Vietnam is a socialist one-party state. However, the country has actively pursued free market economic reforms "Doi Moi "or renovation strategy from 1986. Since launching the reform towards a market economy, the country has maintained relatively high rates of economic growth ranging from 8% in 1989 to 9.3% in 1996.

The *doi moi* reforms have focused on five broad areas (Miller et al, 1996), namely:

1. reform of land use rights;
2. regulation and liberalisation of direct foreign investment;
3. managerial reform in state-owned enterprises;
4. reform of pricing policies and mechanisms; and
5. currency devaluation.

Since the launch of the economic reforms, state subsidies to industry have been cut, price controls have been reduced,

private enterprises have been allowed to compete with state and collective enterprises, and new foreign investment policies have been introduced to attract foreign capital. The dynamic market forces unleashed by these reforms have helped to boost Vietnam's economy.

The turning point in the shift to a market economy is the abolition of numerous government planned compulsory targets and price controls. Universal pricing control is gradually being reduced and market-based pricing is taking over.

The government has shifted focus from direct pricing control to a more analytical role in the valuation of goods and services. However, the state is still responsible for setting the prices of certain essential and/or monopolistic products and services such as electricity, health services and textbooks. Currently, the government Pricing Committee (GPC), which reports directly to the Prime Minister, helps the government regulate prices by establishing minimum and maximum levels of pricing for various products, including machinery, cement, electricity, petroleum products, land use rights, buildings and chattels.

Prior to 1992, the GPC is a single Ministry known as the State Pricing Commission which was fully responsible for setting the prices of most commodities. The country's shift from a centrally planned economy to a market-based economy has thus led to fundamental changes with regard to price control.

In Vietnam, as in other communist countries such as China, all land technically belongs to the state. Following *doi moi*, land use rights reform has been aimed at establishing greater security of land tenure such as through long term allocation of land use rights and through turning land use rights into a legitimate market commodity that can be exchanged, transferred or mortgaged. Such land use rights may in certain cases, such as in the Export Processing Zones (EPZs) and Industrial Zones (IZs), be sublet, subject to permission being granted by the Vietnamese government.

To encourage foreign investments in Vietnam, foreign corporations are permitted to set up representative offices, enter into business co-operation contracts or joint venture with Vietnamese partners, and for certain sectors of the economy, obtain a license to operate as a 100% foreign-owned enterprise in Vietnam. With the introduction of Foreign Direct Investment (FDI) in Vietnam, there is a requirement by both the state and foreign investor, as well as lending institutions, for the determination of the value of contribution provided by the Vietnamese and foreign partners.

Another major feature of *doi moi* has been the government's commitment to the "equitisation" of Vietnam's State-Owned enterprises (SOE's). Under this policy, shares can be offered to workers of the enterprises affected, while the government retains some degree of ownership, and other shares may be sold to outsiders, both Vietnamese and

foreigners. The government uses the term equitisation rather than privatisation which would imply a full loss of ownership/control. As at 1990 there were some 12,000 SOE's in Vietnam. This number has been reduced to below 6,000, of which some 2,000 are controlled by the central government, with the remainder under provincial or district-level authorities. The government plans to eventually equitise most of the remaining SOE's.

The establishment of a market, albeit a limited one, for the transfer and mortgage of land use rights, the introduction of Foreign Direct Investment (FDI) projects largely through joint ventures between the state and foreign investors and the equitisation of State Owned Enterprises (SOEs) among others, have given rise to the need for the service of valuers. Valuers are needed to value the assets, including plant and machinery, which are being transferred, exchanged, mortgaged, contributed in joint-ventures or sold in the form of shares under the programme to equitise SOEs. Hitherto, the services and expertise of valuers as is understood in open market economies were, like in China before its open-door policy, unheard of in Vietnam.

3.0 PROPERTY TENURE AND LAND USE RIGHTS

Under the Constitution and Land Law of 1993, all land in Vietnam belongs to the people under the exclusive administration of the state. As all land is owned

collectively by the people, no individual or organisation may own land. Freehold title is thus not available. However, land use rights in the form of Land Use Certificates can be granted by the relevant level of the People's Committee. These legal rights are guaranteed by the state. The state may also allocate land to organisations and individuals by means of a lease of land use rights and foreigners may lease land.

Enterprises with foreign invested capital may obtain land use rights either by virtue of a Vietnamese party in the enterprise putting up such capital as part of the total capital contribution of the joint venture, or through a land lease approved by the Ministry of Planning and Investment (MPI). Foreign investors must specify the purpose of the land use in the feasibility study which must accompany the application for the investment licence, and any subsequent change of use must be approved by the MPI.

The allocated land use rights, subject to various specific guidelines and conditions, may be transferred, exchanged, assigned, mortgaged, leased or sub-leased. Grantees and lessees of land use right, including foreign lessees, are largely understood to be only entitled to mortgage the value of such land use rights to Vietnamese banks. Any change in the use of the land allocated will have to be approved by the relevant People's Committee. Foreign investors are permitted to construct and re-lease infrastructural facilities together

with the underlying land in Export Processing Zones (EPZs) and Industrial Zones (IZs). Such sub-lessees are, however, not allowed to exchange, assign or sub-lease the land use rights.

The period for which land use rights may be allocated depends on the type of land and lessee involved. For instance, rights for land used for planting annual crops may be for a period of up to 20 years, while rights for land used for perennial crops may be granted for up to 50 years. Vietnamese households and individuals are allocated land for "long-term use". The duration of the land use rights granted to foreign investors is stipulated by law to be a maximum of 70 years, with leases typically lasting between 20 and 50 years. The lease term stipulated in the land use certificate is normally the same as the term of the investment license. However, foreign diplomatic offices and consulate offices may receive a single lease term of up to 99 years.

All land in Vietnam is classified into six categories namely:

- agricultural land;
- forestry land;
- rural residential areas;
- urban land;
- specific purpose (specialised) land; and
- unused land.

4.0 LAND USE PAYMENTS, RENTALS AND OTHER FEES

Depending on the type of land use, the land user must pay certain

land use payments, rentals, land tax, cadastral and other fees.

Land use payments are calculated on the basis of the land area which is granted, or for which a change of purpose is permitted. No land use rights certificates or permits to change the purpose of land use will be issued prior to the payment of the relevant land use fee. When land is leased, the land user is liable to pay land rent instead of land use fees.

The Government has issued nationwide Standard Land Price Tables based on which local authorities issue land price or rental which rate ranges applicable in their respective localities, and within which detailed a payment or rentals which may be agreed by the parties respectively. These are applicable only for transactions with Vietnamese individuals and organisations. The land rentals payable by foreign investors are computed based on a different set of published tables.

For land which is leased to foreign investors, a land rental is paid twice annually or in a lump sum. The basic land rental rates are fixed for a maximum period of five years. The Ministry of Finance (MOF) reviews these basic rental rates every five years and publishes them in a Regulation. However, any increase in rent is subject to a maximum of 15% of the previous rates. The competent authorities use the published basic land rental rates to determine the precise rate applicable for a specific project. The land rental rates are fixed taking into account the location of the land, infrastructure provided,

the total floor area to be built, the number of storeys of the project, the approved use of the land and the objectives of the project.

Foreign investors who pay the rent in one lump-sum in advance for the entire duration of the project will not be subject to the five-yearly rental reviews. In addition, the rental rates for such foreign investors will be reduced by 15% for projects lasting more than 15 years, 10% for projects between 5 and 10 years and 5% for projects with a term of 5 years.

In addition to land use payments, land tax may also be levied on land used for dwelling or construction of project works. According to Decree No 94/CP on Land and Housing Taxes, enterprises with foreign invested capital, including enterprises with 100% foreign-owned capital, shall pay no land and housing taxes during the term of the lease contract, provided the land rent has been paid.

The criteria for calculating the land tax are the surface area and the category to which the land in question is classified. The tax rates on the land in cities, towns and rural residential areas are from 3 to 25 times the highest agricultural tax rate in the region. In the case of a joint-venture investment project, a Vietnamese partner is liable to pay the land tax if the contribution is in the form of the right to land use.

5. FOREIGN INVESTMENT IN REAL PROPERTY

Foreign investment in real

property, in addition to being governed by the *Land Law* and its subsidiary implementing regulations is governed by a separate body of legislation specific to foreign investments in Vietnam, chief of which is the *Law on Foreign Investment*.

5.1 Property Purchases

While all land in Vietnam belongs to the state and anyone can only acquire a right to use land, Vietnamese individuals, organisations and entities, which include joint ventures between Vietnamese and foreign parties, can own buildings on the land. However, foreign persons and individuals are not permitted to own commercial premises. Under a decree issued in 1994, a foreigner may own a house for use as his official residence in Vietnam but only for the duration of his investment or long term residence in Vietnam. Foreigners, after leaving Vietnam for three months lose the ownership of the property, with the state-owned agencies being the only purchaser permitted. Few foreigners have thus purchased properties due to the unfavourable restrictions.

5.2 Property Leasing

Foreigners are allowed to lease properties for dwelling and business purposes from Vietnamese individuals or organisations (including joint ventures) if they possess an investment licence issued by the MPI or a reference letter from a state management department at or above the provincial level or the like. The properties that may be leased include independent

premises (villas) and flats or separate rooms which contain the necessary facilities, dividing walls and independent access to adjoining streets. Vietnam's property laws generally do not permit a sub-lease. Hence, a corporate tenant of an office building cannot rent, say two floors, one for its own use and another for sub-lease until the business expands into it. Tenants thus generally only lease as much space as they presently need with about 10% extra for future growth. Pre-commitment to space in a building which is currently under construction is also minimal, as a property cannot be leased to a foreigner until a building completion certificate is obtained.

5.3 Property Development

Foreign investors may acquire interest in real estate in Vietnam through any of the following forms:

- the Joint Venture Company (JVC)
- the Business Co-operation Contract (BCC)
- the Enterprise with 100% Foreign-Owned Capital (EFOC)
- the Build-Operate-Transfer (BOT) project

A Joint Venture Company (JVC) is an equity joint venture constituting an independent legal entity with a specified amount of paid-up capital, limited liability, and its own board of directors. JVCs are the most commonly used form of investment vehicle in the real estate sector and are preferred for developing commercial, office, residential and recreational properties.

A Business Co-operation Contract (BCC) is a contractual relationship which does not constitute a new legal entity but which is licenced to engage in business activities with respect to a specific project in Vietnam. BCCs have been used in real estate development projects. However, they are not as popular as JVCs due to various drawbacks to the foreign party, such as the higher risk exposure since a BCC is not a limited liability company.

An Enterprise with 100% Foreign-Owned Capital (EFOC) is a wholly foreign-owned subsidiary constituting an independent legal entity with limited liability under Vietnamese law. Only a handful of EFOC's have been involved in real estate. This is likely to be due to the various restrictions imposed on foreign ownership of real property as well as the need for some local market knowledge and experience particularly in real estate investments.

A Build-Operate-Transfer (BOT) project may be structured in essentially the same way as a JVC, BCC or EFOC. However, in the case of a BOT, the Vietnamese party to the relevant contract is a government entity, ownership of the assets of the BOT entity is to be transferred to the Vietnamese Government at the end of the project, and the project relates to infrastructure. Hence, this form of investment in real estate is limited.

Foreign real estate developers have been particularly active in establishing industrial and export processing zones, as well as in

developing specific sites within them. Export Processing Zones (EPZs) and Industrial Zones (IZs) are designated areas located close to or around key cities, and which have been given a separate set of investment regulations that help to speed up the approval process of foreign investors who wish to operate within these zones. Tax holidays and other incentives are also offered to investors within these zones.

There are currently about 30 licenced or planned EPZs and IZs in Vietnam. The two types of zones differ mainly in that EPZs, which were created earlier, are designed to boost exports and consequently, the incentives offered are structured accordingly. Unlike, IZs, EPZs are not permitted to sell to the domestic market. The exclusion from the domestic market has contributed to the lack of investor enthusiasm in the EPZs. In contrast, IZs have performed well. In early 1997, the Vietnam-Singapore Industrial Park (which was licenced in 1996) was permitted to licence foreign-investment projects within its boundaries. This park, in Binh Duong, near Ho Chi Minh City, is the first IZ to be given such authority under a 1996 revision to the Foreign Investment Law. Developers in IZs are allowed to sub-lease the land within the zones after they have catered for the infrastructure such as roads, sewerage, water and power supply in the zone. The land use right is however, not transferred to the operator, which receives only a secondary concessionary

right to use the land. The term of the sub-lease is typically for 45 to 50 years. The land rent is generally payable up front, although it is possible to negotiate for annual payments in some zones. The land rent charged for the sub-lease varies depending on the amount of infrastructure invested by the developer as well as the additional facilities that may be offered.' These could include assistance by the developer to help secure an investment licence for the potential sub-lessee.'

Besides investing in EPZs and IZs, foreign real estate developers, particularly those from the region such as Hong Kong, Taiwan, Japan and Singapore, have also invested in residential, commercial and hotel projects in Vietnam. These tend to be concentrated in Ho Chi Minh City, Hanoi and the areas close to them.

6.0 VIETNAM'S PROPERTY MARKET

While the economy has made progress since its restructuring under the policy of *doi moi*, Vietnam's real estate sector

1. The Vietnamese Government disappointed with the failures of many EPZs have decided after the cancellation of the licence for the Haiphong EPZ in 1995 not to approve any more EPZs. Some of the EPZs have applied for and obtained approval to change their status to IZs in the hope of sparking some foreign investor interest.
2. Land rents charged on sub-leases differ quite substantially among the EPZs and IZs. For instance, Danang IZ charges US\$42 per sq.m for a 50-year lease while the Tan Thuan EPZ, which is a more successful EPZ located near Ho Chi Minh City, charges US\$108 per sq m. as at September 1997 for a lease which terminates in September 2041 (EIU, 3rd Qtr., 1997)
3. The land can only be subleased to the foreign investor if he obtains an investment licence to operate within the zone.

remains small and underdeveloped, with projects of international quality only emerging in the last few years. This may be attributed largely to the many restrictions imposed on property ownership and transfer as well as on leasing and sub-leasing, particularly on foreign investors. Grantees and lessees of land use rights are only entitled to mortgage their land use rights to Vietnamese banks. Pure mortgage financing is still rare in Vietnam. This has further hindered the development of the real estate market since, investors will have to possess adequate financial resources to fund their investments in Vietnam or be able to find alternative sources of financing.

Vietnam's real estate sector is largely concentrated in the country's two key cities Hanoi and Ho Chi Minh, and the areas around them, including the EPZs and IZs. The sub-markets which are active are the office and residential sectors together with the IZs that cater mainly to foreign investors and joint ventures between Vietnamese and foreign parties. The property market catering to the Vietnamese is largely inactive since Vietnam's GDP per capita remains low at about US\$300 as at the end of 1996. It is also generally felt that local businesses cannot yet afford international standard property (EIU, 1st Quarter, 1997).

By far, Ho Chi Minh City has Vietnam's most developed and thriving real estate market. It is Vietnam's leading commercial and financial centre. As at the end of 1996, the city accounted for over 65% or some 1,300 of total

representative office licences issued in Vietnam and over 630 licenced joint venture projects between Vietnamese and foreign firms. Both Ho Chi Minh City and Hanoi are experiencing the addition of a significant amount of new office space and there are some pressures on rentals to decline. Average net monthly rental of prime office space in Ho Chi Minh City was estimated to be US\$32 per sq.m per month as at March 1997, while that in Hanoi was estimated to be US\$35 per sq.m per month (EIU, 2nd Qtr. 1997). It is estimated that Ho Chi Minh City has some 1,76,000 sq.m. of office space as at the end of 1997, while Hanoi has some 50,000 sq.m.

The number of exclusive service apartments catering to expatriates is also experiencing a significant increase in supply. This reflects a shift away from the more traditional villas and hotels previously favoured by foreign executives in Vietnam. In tandem with stagnant growth in expatriate housing population over the last two years, the housing boom has increased competition among new service apartments, hotels and villas which are all competing for the same pool of tenants.

Despite the glut, rentals have not been significantly affected and a new apartment in the city centre can still charge as much as US\$6,000 per month. The number of international standard residential apartments in Ho Chi Minh City as at the end of 1997 is estimated to be 1,210 while the number in Hanoi is 1,075.

Besides the office and residential sectors, foreign real estate developers are also involved in the retail and hotel developments. Projects which recently commenced construction include Diamond Towers in Ho Chi Minh City, a US\$60 million joint venture between British Virgin Islands-registered Woodville Developments and Saigon Jewelry. Diamond Tower scheduled for completion in 1999 will comprise a hotel, shops, offices, apartments and entertainment facilities. While the level of international investment peaked in 1995, Vietnam continues to attract significant levels of foreign investment, albeit at a slower pace, particularly due to the recent regional crisis.

7.0 VALUATION NEEDS

7.1. Public Sector Valuations

While the real estate market in Vietnam remains relatively small and underdeveloped, the demands for valuation, particularly in the public sector is substantial. This arises mainly out of the government's economic reform efforts under the policy of *doi moi*. In the public sector, valuations are required, among others, for the following purposes:

1. to enable the state to manage, distribute and utilise state resources (national assets) more effectively;
2. to determine the value of minerals for proposed mining or drilling projects;
3. to support financial institutions that require the

- assets to be valued for mortgage purposes;
4. to support the transfer of state properties in business co-operation contracts and joint ventures and to determine the value of contributions by the state and the foreign investor in such projects;
 5. to equitise state owned enterprises;
 6. to determine the value of seized property taken for illegal activities of the owners; and
 7. to determine the value of land use rights and the structure on the land when the state compulsorily acquires private property for infrastructure developments.

As stated in section 4.0, the government has issued through the MOF, nationwide Standard Land Price Tables to determine land use payments and rentals to be paid by Vietnamese⁴ to the state for domestic transactions. The land prices stipulated in the Land Price Tables form the basis on which the local authorities issue local land price or rental rates ranges. The land prices are fixed within broadly defined land use, quality and location for the entire country. For instance, urban land is graded into town classes 1 to 5 which are again sub-divided, as the case may be, into three or four street categories. Local authorities are to fix detailed payments or rentals within these ranges. They are also given the direction to multiply the land price with a coefficient of between 0.8 and 1.2.

This is to reflect the different degree of profitability of the land and the state of completion of infrastructural facilities.

Due to the very broad categorisation of land under the Land Price Tables, it is obvious that valuation expertise is still required in order to objectively determine the specific rate to charge for the land.

The Government has also stipulated the basic annual rental rate for the lease of various categories of land to foreign investors such as urban and non-urban land. The rent payments for leases land is computed as:

$$\begin{aligned} \text{Rent} &= \text{Standard Rental Rate} \\ &\times \text{Location Coefficient} \\ &\times \text{Infrastructure Coefficient} \\ &\times \text{Industry Coefficient} \end{aligned}$$

The standard rental rates for urban land are divided into 5 groups based on cities and towns. For instance Ho Chi Minh City

and Hanoi are classified under Group 1 and standard rental rates are the highest at US\$170 per sq.m per annum to US \$13.60 per sq.m per annum. Group 2 comprises three cities, namely, Vung Tau, Bien Hoa and Haiphong, while Group 3 comprises 12 smaller towns. The information is shown in Table 1: The location, infrastructure and industry coefficients range from 1.0 to 2.0. For instance, the location coefficient for a property located in the downtown, in close proximity of cultural, tourist and entertainment centre and with street frontage is 2.0. An industry coefficient of 2.0 is applicable to locations which have all four conditions as stipulated in the relevant regulation on rental rates. Table 2 provides information on the location coefficients as provided in Regulation No. 1417.

Minimum rental rate of fixtures are also stipulated. This is basically to prevent tax evasion by means

Table 1: Rental Rates for Urban Land Published under Regulation No. 1417

Group	Cities and Towns	Rental rates in US\$/sq.m per annum
1.	Ho Chi Minh City, Hanoi City	1.70-13.60
2.	Vung Tau, Bien Hoa, Haiphong	1.50-12.00
3.	12 towns including Hue, Dan Nang, Nha Trang, Can Tho, Da Lat	1.125-9.00
4.	18 towns including Nam Dinh and My Tho	0.75-6.00
5.	Other towns	0.375 3.00

Source: CCH Asia Ltd. and Regulation No 1417

4. Land rentals for local and foreign investors are governed by different regulations

Table 2: Location Coefficients for Urban Land Published under Regulation No. 1417

Location	Location Coefficient
Downtown, street-front, nearby cultural, tourist and entertainment centres	2.0
Downtown but not street-front	1.7
Near downtown, street-front	1.3
Near downtown, not street front	1.0

Source: CCH Asia Ltd and Regulation 1417

of false declaration. Such rentals, unlike land rentals, are typically not paid to the state but by the tenant to the landlord. For instance, minimum property rental rates applicable to foreigners residing in Vietnam for a period of more than six months are published. The rates vary according to the classification of the cities in which the property is located, such as Town Classes 1 and 2 and whether it is in the Central, Near Centre or Fringe of the town. The type of property (villa, detached house or residential block) and the type of accommodation (primary, subsidiary or other areas such as swimming pool) are also taken into account in determining the minimum rental rates.

The government, through the MOF, also stipulates standard minimum prices for newly-built properties as a basis for the computation of compensation to be paid to tenants that are to be relocated due to property development projects. The minimum prescribed prices vary depending on the category into

which the property is classified. There are 8 specified categories ranging from Villa, Classes 1 to 4 and House, Classes 1 to 4. However, the prices of old houses have to be computed using a formula which takes into account the floor area of the house, construction price, age of the house and the expenditures incurred on the house.

As part of its economic reform, the government is gradually selling state-owned houses to existing tenants. Decree No. 61/CP on Purchase and Sale of Housing stipulates the general composition of the sale price for state-owned residential houses as the total of house price and residential land price at the time of the transfer. The house price is calculated based on the residual value. This is in turn based on the length of use and the actual condition of the house and a so-called user value adjustment coefficient which differs according to floor height. Guidelines for valuation of state-owned residential housing are established by the Ministries of Construction, Finance and the

Government Price Commission. The following formula is prescribed:

$$\text{Actual House Value (in VND)} = \text{Actual Quality Ratio (in\%)} \times \text{Original House Price (i.e. new house price in VND per sq m. used area)} \times \text{Area In Use (sq.m)}$$

The quality ratio is defined as a percent ratio of "actual quality" to the "original quality".

In all of these cases, valuers are required to periodically review the stipulated minimum prices of newly-built properties, the Land Price Tables, land rental rates and the minimum residential property rental rates for foreign investors, in order to reflect changing market conditions. In addition, valuation expertise is also required to determine the detailed land price or rents for each specific parcel of land within the stipulated rates.

The Government, through the GPC, is also often required to provide valuation of real assets, including plant and machinery, where a joint venture or a business co-operation contract is undertaken with a foreign investor. The usual breakdown in ownership is about 30% from the Vietnamese partner and 70% from the foreign investor. The Vietnamese partner usually contributes the land use rights, as well as local knowledge. The foreign partner contributes "technology", plant and machinery and equity. The Government needs to value the contribution of the foreign investor as well as the contribution of the Vietnamese partner in order to ensure that the

joint-venture is viable and equitable.

7.2 Private Sector Valuations

In the private sector, valuations of real estate assets are mainly needed for:

financial reporting purposes; the purpose of obtaining loans from financial institutions; public listing of the foreign investment company in their country of origin; and studies on the investment viability of the project.

Valuers are also often called upon to undertake feasibility studies of proposed real estate development projects in Vietnam by the Vietnamese or foreign parties.

It may then be seen that among others, state management in areas of foreign direct investments in Vietnam, privatisation of state-owned enterprises and management of state capital and assets in enterprises depend very much on properly conducted valuation. The Government is eager for its officials to acquire valuation skills as it is ambivalent of the fact that foreign investors may overvalue their stake in the joint-venture, such that the Vietnamese partner may be required to provide far more equity than would be required if proper valuation methodologies were used. At the same time, foreign investors would also require fair appraisal of the land use rights and other assets contributed by the Vietnamese partner. In the case of real estate

developments, the foreign investor would require a feasibility study of the project in order to determine its viability.

8.0 VALUATION METHODOLOGIES

Although the Ordinance on Domestic Land Users provides that the land use rights vested in Vietnamese individuals and organisations may be transferred by exchange, assigned, leased or sub-leased, in effect only certain transfers by lessees are permitted.

Grantees of land use rights may not exchange, assign or lease their land use rights. In addition, sub-lease of land use rights by foreign investors is only permitted in the case of land in the EPZs and IZs. Moreover, every foreign investor who wishes to lease land from the developer of the EPZ or IZ has first to obtain an investment licence from the government and no further sub-lease is allowed. The market for land use rights is thus limited.

As noted in section 6.0, the property market catering to the Vietnamese is largely inactive due to the restrictions on transfers of land use rights as well as structures, and the lack of purchasing power as the per capita GDP remains low at about US\$300 as at the end of 1996. Vietnam's real estate market is thus still small and underdeveloped and there is very little evidence of sales transactions. Most of the activity in the real estate market is in property development and the leasing of completed spaces to

foreign investors.

Valuations undertaken in the private sector are largely for financial reporting purposes, for inclusion in prospectus for the public listing of the company in its country of origin or for determining the viability of proposed developments. These valuations are largely commissioned by foreign investors and undertaken by international valuation firms with offices in Vietnam.

The projects which re-valued are generally large commercial complexes like industrial properties, office buildings, shopping centres, hotels or mixed developments. Such properties tend to be valued based on the income approach due to the absence of sales prices of comparable properties. The choice of a capitalisation rate to be applied does, however, pose some problems. To derive rates, valuers have to consider the required rate of return of their clients as well as the known yields of similar quality properties in other countries in the region. For instance, a valuer undertaking the valuation of an office development in Vietnam using the income approach may apply a capitalisation rate in the range of 12% to 15% based on the investor's required rate of return as well as known yields of 6% to 8% in less risky countries in the region, such as Malaysia. The income approach utilised could use the conventional capitalisation technique or the discounted cash flow technique. The direct comparison method can only be

used to determine the rental rate that is applicable for the development being valued. It is hardly used in capital valuation since there is a dearth of comparable property sales in Vietnam.

In the public sector, the replacement cost approach appears to be the most commonly used method of valuation. In one instance, it was observed that a quantity surveyor was asked to estimate the costs of construction of a hotel as of a given date in order to determine the contribution that should be paid by a foreign investor who wishes to acquire an equity stake in a completed development together with a Vietnamese party. The contribution that should be made by the foreign investor would have been more appropriately determined based on the income approach than by the cost approach. This points to a lack of understanding of valuation principles and concepts, particularly in the public sector. Notwithstanding the foregoing, it is understood that the government valuers have started using the income approach as a method of valuation, particularly in determining the value of contribution made by the Vietnamese party (in most cases the government) and the foreign party.

In the standard minimum prices for newly-built houses published by the Ministry of Finance, house prices are calculated based on construction cost and construction area. The valuation

of plant and machinery is largely based on the cost approach. However, it was noted at two valuation training courses recently conducted in Vietnam,⁵ that the concepts of replacement cost and accrued depreciation, due not only to physical but also functional and economic obsolescence were not well understood. For instance, a question was asked as to whether the historical cost of a machine, which was purchased some five years ago, could be adopted at its value as it has never been used since it was purchased five years ago.

9.0 VALUATION ISSUES

Valuation is a new discipline in Vietnam and there is currently no established valuation profession in the country. The lack of trained qualified valuers in the country, the small and under developed real estate market and dearth of market transactions together with the many legislations that govern real estate development and transactions pose major challenges to the government, property investors and valuers alike. Most of the private sector valuations required by foreign investors are currently undertaken by valuers from abroad, but who are stationed in Vietnam or sent from their home country by consultants with offices in Vietnam. Many government officers assigned to undertake valuations for the state do not possess formal training in valuation. They appear to lack an understanding of the concepts and operations of a market economy. This was reflected by

the kinds of questions asked by government officers at two valuation training courses recently conducted in Vietnam by the author and other lecturers from the School of Building and Real Estate, NUS. For instance, a question was asked as to whether the value of two properties, one located in the city and another in the suburb, would be the same if the improvements on both plots of land are similar and constructed at the same cost.

There is a dearth of market transactions of real estate in Vietnam due to the various restrictions imposed on the transfer and lease of land use rights and improvements on land. There needs to be further deregulation of the real estate market in order to allow for its growth and development. Restrictions imposed on mortgage loan financing, sub-leasing, sale etc, should be re-evaluated since such policies fetter the development of the real estate market. As the market develops and matures, there would also be a need to further refine, among others, the published standard land price tables, land rental rates and minimum prices for newly built houses in order to better reflect the heterogeneity of real estate. Currently, the land and building classifications used in the tables tend to be very broad.

5. In July 1997, the author, together with 3 other lecturers from the School of Building and Real Estate, National University of Singapore (NUS), conducted a three-day valuation training course for some 400 government officers in Hanoi. In December 1997 a similar training course of some 300 government officers was conducted in Ho Chi Minh City.

10.0 DEVELOPING THE PROFESSION

The Vietnamese government recognises the importance and need to develop the valuation profession in the country in order to further strengthen its transition from a centrally planned economy to market-based economy.

As a first step towards this direction, the Government Pricing Committee acting as a representative of Vietnam was given approval by the Prime Minister of Vietnam to become a member of the ASEAN Valuers Association (AVA) on 12 June 1997. Plans are also underway for the establishment of a Vietnam Valuation Centre for training valuers as well as for undertaking valuation work. A project on developing the valuation capacity of the Vietnamese Government, which is being funded by the UNDP, and supported by several key Government Ministries, including the Ministry of Planning and Investment, Ministry of Finance and Ministry of Foreign Affairs, is underway.

The government also plans to spearhead the formation of a professional organisation for valuers in Vietnam under the auspices of the GPC. To promote professionalism in the industry, legislation relating the practice of valuers as well as valuation standards, guidelines and practice notes are to be instituted.

On the valuation training programmes as well as valuation training courses and seminars are being organised by the GPC to

train government personnel involved in valuation work. The GPC has two colleges under its wing which would be used to implement the training programmes. These are the College of Business Administration (Formerly Pricing College) in Hanoi and the College of Marketing in Ho Chi Minh City. Diploma level valuation courses are also being organised at the two training centres. The Vietnamese government has asked its ASEAN neighbours to assist in developing the valuation profession in Vietnam through training courses to be conducted in the sponsoring country. For instance, the Singapore Government, through its Technical Assistance for IndoChina Scheme, sponsored a one-month valuation training course in Singapore from 16 March 1998 to 11 April 1998. The course was conducted by the School of Building and Real Estate, NUS. There are also plans to develop a University degree level course at the National Economics University in Hanoi.

The Vietnamese government's efforts to develop the valuation profession is indeed commendable. Since the profession is in its infancy in Vietnam it is appropriate for the government to spearhead plans to develop the profession at this junction. When the profession has developed sufficiently, it could be allowed to become more autonomous and assume more responsibilities to enhance the standards of the profession. Based on the experience of the valuation profession in many

countries, properly drafted legislation, valuation standards and practice notes are the most effective way to ensure professionalism in the industry, as well as to protect the interests of the public who use the services of valuers. In view of the globalisation of real estate, internationally recognised value definitions and practice standards, such as the International Valuation Standards published by the International Valuation Standards Committee (IVSC), should be adopted.

11.0 CONCLUSION

This paper has highlighted the role and potential of valuers and valuation in an emerging market economy, Vietnam. In many respects that are still unnoticed to the outside world, Vietnam has succeeded in finding a middle ground between the traumatic political reforms of the former Soviet Union and the more purely economic reforms of China, creating what it hopes will be a stable foundation for long term growth and prosperity (Chu, 1994). This statement also largely mirrors the state of the valuation profession in Vietnam. Although still in its infancy, the Vietnamese government has recognised the need to nurture the profession and plans are underway to develop it. However, it is noted that there are currently various problems that confront the valuer when undertaking valuations in Vietnam, such as the lack of market transactions and information, and the many legislations which govern real estate investment and

development that a valuer needs to understand. In addition to implementing legislations, policies and projects to develop the valuation profession, the various restrictions imposed, among others, on the transfer of land use rights and property by both locals and foreigners, and mortgage loan financing, should be reviewed, and where possible lifted. This would enable the property market to develop and grow, thus further enhancing the objective of Vietnam to shift away from a centrally planned economy to a market economy.

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Cross Border Valuations

with particular reference to
PLANT and MACHINERY
and to the
INVESTMENT by FOREIGN
INVESTORS in LOCAL
COUNTRY JOINT
VENTURES

GraemeHorsley FNZIV

INTRODUCTION

In this article, originally presented as a paper at the 19th Pan Pacific Congress of Real Estate Appraisers, Valuers and Counselors in Singapore during April 1998, Graeme Horsley shared his views and experiences as a valuer, who has been involved in the establishment and continued revising of valuation standards appropriate for cross border valuations.

Throughout the world, companies need to prepare financial statements to meet local capital market financial reporting requirements. For many of these companies, one of the principal items of the financial report will be fixed assets. This includes property, plant and machinery. In the past, accounting policies throughout different countries

have not been standardised and this has caused confusion, particularly where current valuations of fixed assets are concerned. The treatment of plant and machinery has been especially inconsistent in developing or newly industrialised countries. While international valuation standards are important for cross border financial reporting, they are also important in the standardisation of plant and machinery insurance valuation. Newly industrialised countries, those countries that are now experiencing industry expansion and significant foreign investment, will benefit significantly from international accounting and valuation standards.

"The large recent inflows of foreign direct investment and the equitisation of state owned

This paper was presented at the 19th Pan Pacific Congress held in Singapore in April of this year.

enterprises have dramatically increased the need for plant and machinery valuers and associated valuation professions in many newly industrialised countries. "

At present, many newly industrialised countries have inconsistent financial reporting policies and little, if any, valuation standards. In fact many don't even have recognised professional valuation bodies or satisfactory valuation training.

In this address Horsely discussed the development and requirements of international accounting standards and international valuation standards. He looked at the requirements of plant and machinery valuation with regard to financial reporting and insurance. Finally, he discussed the valuation methodologies that should be applied in plant and machinery valuation, looking specifically at cross border transactions and differences between cost and value.

Accounting Standards

In the past most countries had accounting standards that contained specific requirements with regard to the financial reporting of fixed assets.

However, these were often inconsistent with other countries accounting standards and further did not make adequate provision for the role of valuation in financial reporting.

The International Accounting Standards Committee (IASC) was

formed in 1973 to standardise international financial reporting and to publish International Accounting Standards. Members of the International Federation of Accountants (IFAC) make up the IASC. This includes 110 Member bodies in 82 countries who represent over one million accountants. Ernst and Young is an active member throughout the world on this committee.

One of the objectives of the IASC is to harmonise as far as possible the diverse accounting policies of different countries. For example, presently, even developed countries have different accounting practices in regard to real assets.

The objective of financial statements is to provide information about the financial position, performance, and changes in financial position, that is useful to investors in making investment decisions.

Standard financial accounting, across international boundaries, allows uniform measurement of financial performance and the financial position of investments throughout the world. Investors can analyse investments without the confusion and discrepancies that exist where accounting policies between countries differ.

Many foreign investors, involved

International Property Accounting Differences

United States	Conservative Market Value
Japan	Book Value
Hong Kong	Conservative Market Value
New Zealand	Market Value
United Kingdom	Market Value
Germany	Lowest Book Value
France	Book Value

Source: Goldman Sachs Global Research

Why do foreign investors need standard accounting reporting?

Foreign investors are the providers of risk capital in joint ventures. As such, they are concerned with the risk, and the return on their investments. Investors need information to help to determine what the foreign investment's performance has been and how that measures against other investments in other countries.

in joint venture operations in newly industrialised countries, are currently experiencing such confusion because local accounting policies are either outdated or differ significantly from the accounting policies in developed countries. Most developed countries have established local accounting standards which mirror the International Accounting Standards. Where cross border valuations are required, standard

financial reporting is almost a necessity. It helps foreign investors accurately assess their true and fair investment worth for each foreign joint venture investment.

The IASC has issued 29 International Accounting Standards which have been effective from 1 January 1995. These standards deal with the majority of topics that affect the financial statements of business enterprises. The IASC concentrated on essential points and has made the standards relatively simple so that there is ample leeway to apply the standards effectively throughout the world.

The international accounting standards have been used

- As national requirements;
- As a basis for national requirements;
- As a benchmark for those countries which develop their own requirements;
- By regulatory authorities for domestic and foreign companies;
- By companies themselves

The use of international accounting standards is to be encouraged in all newly industrialised countries governments and foreign companies investing in newly industrialised countries. Cross border valuation can only become globally consistent if individual countries meet international accounting standards first. Multinational companies must be able to report all their earnings and

assets on a consistent basis throughout the countries they invest in. The reporting and analysis of assets in one country must be able to be compared to the reporting and analysis of assets in another.

The International Accounting Standards do not override any local regulations that govern the issue of financial statements in a particular country. However, where local regulations require deviation from International Accounting Standards, the local members of IASC try to persuade relevant authorities of the benefits of complying with international standards. As a result more and more countries are bringing their accounting policies in line with the International Accounting Standards.

Accounting for Plant & Machinery

Within financial reports there is the need to place current values on plant and machinery that a company owns and operates. The International Accounting Standard IAS 16 Property, Plant & Equipment puts forward the policies specific to accounting for plant and machinery.

This standard was revised in 1993 following its introduction in 1981. It states that an item of property, plant and equipment which qualifies for recognition as an asset should initially be measured at its cost.

Where the cost comprises:

- Purchase price, including import duties and non-refundable purchase taxes

- Directly attributable costs involved in bringing the asset to working condition for its intended use, these include:
 - a) the cost of site preparation;
 - b) initial delivery and handling costs;
 - c) installation costs;
 - d) professional fees, such as for engineers;
- Any trade discounts or rebates are deducted in arriving at the purchase price

The standard then provides the following two methods to measure an assets value after its initial recognition:

- Cost less any accumulated depreciation (measured against benchmarks).
- Fair value at the date of the revaluation less any subsequent accumulated depreciation.

It is the latter treatment measuring fair value, which introduces the role of the plant and machinery valuer to the financial accounting process.

The fair value of items of plant and equipment is usually their market value determined by appraisal. When there is no evidence of market value because of the specialised nature of the plant and equipment they are valued at their depreciated replacement cost. In determining fair value, an item of plant and machinery is valued on the basis of its existing use. However, an asset for which a change in use is probable, is valued on the same

basis as other similar assets held for the same intended use.

From within the framework laid out in the International Accounting Standard for the financial reporting of plant and machinery the International Valuation Standards have been developed.

Valuation Standards

Throughout the developed world valuation professions have grown to the extent that most have national representative bodies such as the New Zealand Institute of Valuers (NZIV). Many of these bodies have developed standards of professional practice and code of ethics. In addition, many governments have incorporated such standards into national laws and regulations. However, these individual national valuation practices, in many cases, had conflicting methodologies and different viewpoints were leading to unintentional misunderstandings. There was a definite need for global consistency in valuation.

Equally important was the rapid change and internationalisation of business among nations and the increasing recognition of the market importance of professional asset valuations. This has shown itself in the increasing movement towards reporting asset values for accounting and financial purposes on the basis of current valuations in place of historical cost. In addition, growing foreign investment in plant and machinery has seen a greater emphasis on insurance by foreign

investors and the need to have uniform insurance valuations throughout the world. Valuation standards were required which would standardise the role of valuation within financial reporting so that the same valuation principles could be applied across international borders.

The International Assets Valuation Standards Committee (TIAVSC) was founded in 1981 and was set up to produce international valuation standards and further to promote their worldwide acceptance. TIAVSC first published International Valuation Standards in 1985 but have since revised them as late as 1994. International Valuation Standards have been produced in liaison with International Accounting Standards so that not only is valuation globally standardised but the valuation of assets for financial reporting can be consistently applied across international borders. New Zealand is a member of the (now) International Valuation Standards Committee (IVSC) along with many other countries throughout the world. I (Graeme Horsley) am a former Chairman of the IVSC and remain active in such matters as valuation standards both from an international and local perspective.

International Valuation Standards recognise the complexities and diversity of situations that are found throughout the world. They have been written so there is sufficient leeway to modify them for local regulations as

required while still retaining the necessary valuation fundamentals. The standards provide guidelines in these areas:

- Scope to which the standard applies.
- Definitions of the terms used including market value.
- The relationship between valuation standards and accounting standards.
- General valuation methodologies to be used for specific classes of properties.
- Disclosure requirements.

Generally, international and local valuation standards have in the past tended to concentrate more on the property portion of assets with plant and equipment assets mentioned only briefly. In New Zealand the Institute of Plant and Machinery Valuers Inc (IPMV) has developed a set of standards purely for plant and machinery valuers, however, these very much mirror the IVSC guidelines.

IVSC Standard 3, *Valuations for Financial Statements and Related Accounts*, is the most relevant standard for the value of plant and machinery. For the financial reporting of plant and machinery this standard provides that:

- non-specialised assets that are neither investment nor surplus, shall be valued on the basis of *Market Value for the Existing Use*, and
- specialised assets shall be valued on the *Depreciated Replacement Cost* basis, unless *Market Value* can be applied.

International Valuation Standards follow the requirements of the International Accounting Standards and it is clearly shown that plant and machinery should, if possible, be reported according to its market value.

The New Zealand Institute of Valuers (NZIV) have worked with the International Valuation Standards Committee and the New Zealand Society of Accountants over the last few years to increase awareness of the need to adopt the international valuation standards. Many of the inconsistencies between the requirements for financial reporting in accounting standards and valuation standards have been removed in New Zealand and there should now be a greater push to do the same for Newly Industrialised Countries. The International Valuation Standards, if approved and used by newly industrialised countries governments, would help greatly in the consistent valuation and financial reporting of plant and machinery. Any report which does not have reference to the IVSC standards, or to local standards that are based on the international guidelines, should be looked at with caution.

Plant and Machinery Valuation

Now that I have explained the development and requirements of the International accounting standards and the international valuation standards I will take a more detailed look at why plant and machinery valuations are

important and I will discuss what should be provided in the valuation report.

In many developing countries the emphasis of foreign investment has been in industry and production. This creates a huge capital investment in plant and machinery in the developing country, mainly through foreign joint venture arrangements.

"Frequent, sustainable valuations of plant and machinery are an important tool in monitoring the performance of capital in industry investment."

Based on the level of foreign investment in plant and machinery in developing countries the main emphasis of valuation will be with plant and machinery valuers rather than property valuers in the upcoming years. Between 65% and 90% of investment by foreign joint ventures in fixed assets is in plant and machinery. Together with this investment in plant and machinery there is growing need to adequately insure and to financially report asset values. In many countries government regulations specify that valuations of plant and machinery must be undertaken on a regular basis.

The plant and machinery valuer therefore has an increasingly important role in newly industrialised countries with plant and machinery valuation specifically required for financial reporting and insurance valuations.

What a Plant and Machinery Valuation Provides

The plant and machinery valuers role in today's commercial environment is to provide his client with an independent, unbiased, fully researched and logical assessment of the value of that particular client's plant and machinery at a specific date, and in accordance with the clients specific instructions. The valuation should be supported by appropriate documentation and reported upon in accordance with the appropriate international valuation standards and if applicable, local valuation standards and methodologies.

A typical plant and machinery report usually consists of a detailed report letter highlighting all relevant points and a detailed asset schedule.

This detailed report/letter should contain information on the following aspects of the valuation:

- a) A statement of the specific instructions or terms of reference upon which the valuation is to be performed.
- b) A statement of the purposes and function of the evaluation including any statutory criteria which may apply.
- c) A brief description of the nature of the assets which have been valued.
- d) The effective date of valuation.
- e) A clear and reasonable summary of the source of data

upon which the valuation is based, including conclusions from evidence, market conditions, and their application to arrive at the value.

- 0 A clear and reasonable presentation of the valuation method or methods adopted to arrive at the value.
- g) A definitive synopsis of, or a specific reference to, any documents used or referenced, in the valuation process which are relevant to a proper understanding of the valuation report.
- h) A clear statement of any assumptions and limiting conditions associated with the valuation conclusions.

The importance of the Asset Schedule

The asset schedule is the final, and perhaps most important part of a plant and machinery valuation report. The schedule records in detail the plant and machinery which actually exists and has been valued using the appropriate methodology for the valuation requirements.

It may be a surprise to know that the level of accuracy of companies fixed asset schedules is generally low when compared to what physically exists. One of the main reasons for this is that over the years engineers have retired or sold production machines and the information has not been passed to the people (usually accounting) involved in keeping accurate fixed asset registers.

Another reason is that equipment has been purchased, not as capital expenditure, but under maintenance expenditure and, as such, has not been recorded as a fixed asset. This situation is not peculiar to any particular country, industry or size of company given stories told by valuers around the world.

A valuer's fully detailed asset register provides his client with an up to date, accurate, independent schedule of all equipment assets at the client's premises. In the event of a loss by fire, flood, theft or other disaster, this document gives independent verification of the assets existence for insurance claim purposes. In the event of a merger, or take over, it provides the same information to both purchaser and vendor so that all parties know what assets are included within the transaction.

A good asset register will include vital information such as make, size, model, serial number, accurate description and age. There would be few accounting registers that contain as much detail as a valuers fixed asset register.

Consideration was then given to furthering the requirements specific to valuing for financial purposes and those for insurance purposes.

Valuation for Financial Purposes

Valuation for financial purposes covers a wide range of requirements

and includes assessing plant and machinery values for a whole range of purposes such as:

- Company balance sheet.
- Accounting and audit functions.
- Initial public offerings and share floats.
- Merger and Acquisition proceedings.
- Establishing value as collateral for a loan or mortgage.
- Establishing value for local authority rating or tax assessments.
- Receivership and liquidation responsibilities and actions.
- Taxation depreciation claims.
- Verifying that equipment costs incurred during purchase are equitable in terms of accepted market practices in both local and/or international markets.
- Purchase or disposal.

These valuations are performed after receiving instructions from people such as bankers, investors, receivers and liquidators, lawyers, accountants, auditors and joint venture partnerships to name just a few. In line with the international accounting and valuation standards it is expected that any valuation of plant and machinery carried out for financial purposes will reflect the market value of that equipment, as at the date of valuation for whatever 'financial purpose' the valuation is required. It is extremely important for both the valuer and the person instructing to be absolutely clear

on the requirements of the valuation from the very outset of the assignment.

Insurance Valuations

On an international basis the vast capital investment made in newly industrialised countries over the past few years especially in plant and machinery has caused governments and foreign investors to ensure such assets are adequately insured. They have recognised these large investments and the need to safeguard them through insurance of some kind. Vietnam is one country where they have stipulated insurance on people assets in law although, in today's commercial environment it should be considered an absolute necessity anyway.

Internationally there are three main types of insurance valuations for plant and machinery. These are:

1. Indemnity Insurance

This equates to the cost of replacing an existing asset with one of a substantially similar nature in terms of age, productive capability, condition and remaining economic life. To value for such purposes valuers generally use one of two approaches and quite often a mixture of both. These approaches are:

- Depreciated reinstatement new cost
- The cost of acquiring from the market place, a similar age/condition asset plus full allowances for freight, installation and commissioning and any local taxes applicable.

2. Reinstatement with New Insurance

This equates to replacing an existing asset with a completely new asset of identical manufacture, production capacity and size, plus an allowance for freight, installation and commissioning and any local taxes applicable. Values for such purposes are generally obtained from suppliers and or a valuers database.

3. Functional Replacement

This equates to the cost of replacing either a group of, or all, assets within a production facility to perform similar tasks under optimum current design, but with a total capacity not greater than currently exists. Values for such purposes reflect significant changes in technology where, for instance, one new machine can perform the job of ten existing but older and technically obsolete machines.

Indemnity is the oldest form of insurance in the world whilst functional replacement is one of the newest. Probably the easiest basis of insurance, from a valuers viewpoint, is reinstatement with new, as in general terms it does not contain so many judgmental decisions as the other two bases. It also appears to be the most favoured basis of insurance in many countries, in respect of plant and machinery.

Plant & Machinery Valuation Methodology

Obviously the most important part of the plant and machinery report is the value arrived at and

how it was achieved. Historically, the valuation of an item of plant and machinery was done on an accounting cost basis, this was simply the historical cost less depreciation. Following the international accounting and valuation standards, market value should now be adopted wherever possible.

To arrive at a market value for plant and machinery there are two major valuation approaches that can and have been used internationally. These are:

replacement or depreciated replacement cost, or
market/sales evidence comparison.

The use of either approach depends upon factors such as the nature of the plant to be valued, the level of its special purpose construction and use, and the availability of sales evidence for such equipment. These approaches are applicable for most types of financial and insurance valuations, which form the vast majority of a plant and equipment valuer's workload.

It is preferable to employ a replacement or depreciated cost, for insurance valuations. In terms of financial valuations, a mixture of both replacement and market and sales evidence comparison should be used. The mixture of approaches depends solely on the type of equipment being valued and the requirements of the country in which the plant is being valued in. In other words, each individual valuation project

has to be considered as a single task.

Verifying the Cost of Equipment

Many cross border valuations of plant and machinery require the valuer to verify equipment purchase prices. Plant and machinery equipment, in many instances, is highly specialised and may only be produced and supplied by a few companies in a few countries. Other equipment may be common and supplied by many companies in many countries.

To provide accurate valuations requires the plant and machinery valuer to have built up an international network of suppliers and a database of equipment prices. The valuer should have regular contact by phone, fax and email so they are aware of new products, product obsolescence, technological advances and so on. In today's computer age email and the Internet are both powerful tools in reaching suppliers and directly researching machinery products.

In some cases plant and machinery equipment may have been transferred internally within a company or bought by the parent company and on-sold to an international subsidiary. Assessing the price paid may be difficult and in intra-company transactions, transfer-pricing principles may have to be applied to assess the true cost of an item. This cost will then have to be adjusted to assess a true market value of the item at any time.

A transfer price is defined as the price charged by a selling department, division, or a subsidiary of a Multinational Corporation for a product or service supplied to a buying department, division, or subsidiary of the same Multinational Corporation.

"It is inevitable that many parties involved in foreign joint ventures wish to overstate the value of their contribution to maximise the value of their share and avoid taxes."

One way of achieving this is in the internal transfer of assets, within a multinational company, at 'prices' higher than in arms lengths transactions. This is commonly known as transfer pricing, where companies can decrease their total tax liability by increasing tax deductions such as depreciation charges.

Multi-national companies develop transfer-pricing policies to minimise tax and increase their profits in response to the regulations in the countries they invest in. Governments develop transfer-pricing regimes to reduce the loss of tax revenues because of transferring the assets across international borders. Although the OECD has produced international transfer pricing guidelines many Newly industrialised countries have few regulations with respect to transfer pricing in place. Their transfer pricing policies do not usually cover all situations and in many cases are not very effective. In addition, harsh local government regulations may encourage aggressive transfer pricing by international companies.

In the world of plant and machinery it is often likely that companies have transferred equipment within the company across international borders. This makes it extremely difficult to assess the true cost to a company for their plant and machinery.

New Zealand's transfer pricing regime follows the international transfer pricing guidelines produced by the OECD in July 1995. The current New Zealand transfer pricing regime requires that for tax purposes an asset transaction must be assessed as if it was at arms length. One, or a combination of, these five transfer-pricing methodologies must be used to determine such a transaction price.

- 1) Comparable uncontrollable price.
- 2) Resale price method.
- 3) Cost plus method.
- 4) Comparable profit method.
- 5) Profit split method.

The best method rule must be adopted in that the method, or combination of methods, which gives the best result must be used. The method chosen will have regard these factors:

The degree of comparability between the transactions actually undertaken by the taxpayer and the transactions to which they are being compared.

The completeness and accuracy of the data being relied on.

The reliability of any assumptions made; and

The sensitivity of any results

to possible deficiencies in the data and assumptions used.

As the uncertainty of these factors increases, it will become more difficult to apply the appropriate transfer pricing formula and more difficult to estimate an accurate price.

New Zealand's transfer pricing regime attempts to give a true indication of the price or cost of an asset when it transacts. As a plant and machinery valuer one must attempt to find the value of an asset at a particular time. This may be predominately based on the assets cost when it recently transacted. Where there is little market evidence, applying transfer-pricing methods to an internal company transaction may be the only reliable estimate of cost.

Is Cost Equal to Value?

We have discussed finding the appropriate cost or purchase price of an asset, but cost does not necessarily equal value. I have discussed that the International Accounting and International Valuation Standards specify market value for both financial reporting and insurance valuation. The cost of plant and machinery may not be the same as its market value in use. The cost of a piece of equipment, once paid for, becomes historical fact and can never be changed. Its value however, can rise, fall or remain the same, as value is an economic concept and requires many factors to be considered. If, for example, you take a piece of equipment manufactured in

France and install it in Vietnam, its insurance value each year depends on issues such as:

- source country inflation;
- inter-country currency movements;
- labour costs- installation and commissioning;
- freight and insurance.

In addition to these factors there are physical factors which must be taken into account, such as:

- age;
- condition;
- production requirements;
- obsolescence,

The financial value can rise and fall, sometimes annually, when such factors are taken into consideration. However, the cost will always remain the same, because, as I have previously stated, cost is a historical fact. The value of a piece of plant and machinery is likely to be increasingly different from the last transaction price (or assessed 'true' transfer price) as time passes. With all the factors described above that affect value, the transaction price may not reflect the value of the equipment as it applies to its existing use.

Summary

I hope that you all now have a better knowledge of cross border valuation and especially the efforts undertaken by accountants and valuers to create an international valuation methodology that can be used throughout the world. As I have said plant and machinery

valuation is increasing in importance in Newly Developed Countries as the level of joint venture foreign investment grows and the need for companies to insure and financially report it.

"The international accounting and valuation standards are a good platform for Newly Developed Countries to develop their own valuation standards and to establish and advance their valuation professions. "

The international standards have placed increased importance on assessing market values based on market evidence and current economic conditions rather than using historical cost. Multi-national company transfer pricing makes it difficult to assess the true cost in many instances, however, the movement away from historical cost towards market value means less reliance has to be put on a transfer pricing approach.

About the author

Graeme Horsley is well known throughout New Zealand in the valuation profession as a leading practitioner, an advocate of quality standards in the profession and a driving force for the new age Valuer and Property Consultant. He is currently a senior partner in the international practice of Ernst and Young where he is also National Director of Real Estate Services.

Ref. • NZVJ July 1998 page 61

DCF MODEL FOR VALUING LESSOR'S INTERESTS

Reid Quinlan

This article has been prepared to present the lessor's interest valuation model developed by the writer while working on a range of leasehold valuations recently at Seagar and Partners, in Auckland. The formula is a simple discounted cashflow (DCF) method with the flexibility to accommodate a wide range of terms and scenarios. Readers are encouraged to think about further applications of the model in the world of leasehold valuations.

The formula is designed to fit into one cell of a spreadsheet. The advantage is that the varying inputs from different properties can easily be incorporated into a list, and the formula grafted on to that list. In this way, the present value (PV) of all of the individual cashflows from a portfolio can be

calculated with common growth or discount rate assumptions if required.

In order to start, readers are assumed to understand basic ground lease valuation scenarios and will need a computer running the Excel application. Basic spreadsheet skills only are required, sufficient to enter formulae, work with simple spreadsheets, and name cells in a worksheet. Two simple examples are used to illustrate the model, but the model is flexible in that it allows for any combination of rent review frequencies, payments in advance or arrears, term to next review, termination date, and so on.

The two examples are summarised in the following table.

Table 1

Attribute	Property A	Property B
Freehold Land Value	\$1,000,000	\$1,000,000
Current Ground Rent	\$15,000 pa	\$15,000 pa
Basis of Payments	Quarterly in advance	Quarterly in advance
Review Periods in Ground Lease	21 yearly	21 yearly
Current Ground Rental Rate	7% x Land Value	6.5% x Land Value
Term to Next Review	7 years	7 years
Term to Lease Final Expiry	Perpetually renewable	70 years

For these examples a nominal discount rate of 10.5% per annum has been assumed, and a compound annual growth rate of 3% has been applied to the land. Ground rental payments are made quarterly in advance for these examples, so it is necessary to convert the annual nominal discount rate to a periodic (quarterly) compounding discount rate. This is done with the following simple Excel formula:

PRINCIPLE OF MODEL

The market price of any investment property reflects the

present value of all of the expected future cashflows, discounted at an appropriate rate. In the case of perpetually renewable ground lessor's interests, the owner can never expect to regain the unencumbered freehold interest, but has the right to all of the future cashflows. By assuming long term growth rates, it is possible to estimate these cashflows. If assumptions are consistent, then sales of lessor's interests can also be analysed to show the required return (discount rate) of the purchasers. The discount rate is the expected total long term

return from the property, as distinct from a capitalisation rate, or initial yield. Use of the Seagar and Partners' DCF formula is a totally market related approach to valuation of leasehold interests, as it relies on market evidence rather than a 'built up' discount rate from other sources which often appear to be contrived, open to manipulation, or not convincingly derived.

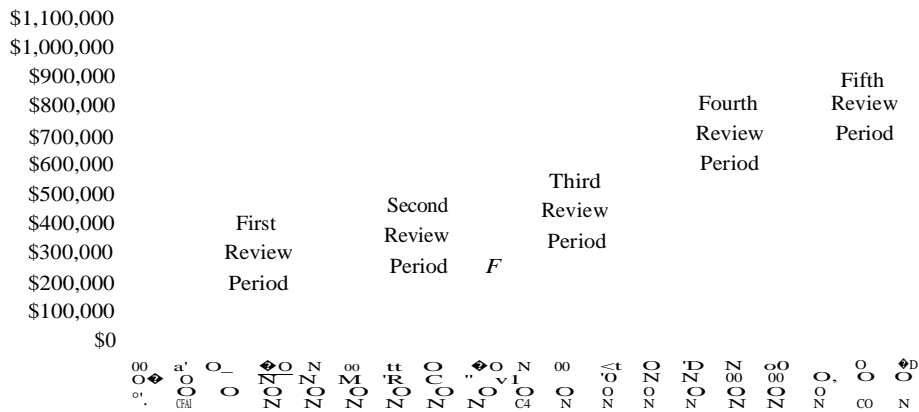
The cashflows from Property A may be forecast to show a pattern like Graph 1.

Discount rate: 10.5% 4 payments
per annum per annum

$$\begin{aligned} \text{Effective quarterly discount rate} &= (1+.105)^{(1/4)}-1 \\ &= 2.52755\% \text{ per quarter} \end{aligned}$$

Graph 1

FORECAST ANNUAL GROUND RENT FROM PROPERTY A



DERIVATION OF THE FORMULA

Similar to traditional methods, the calculations are broken up into two parts:

- A. The present value of the contract income until the next rent review.
- B. The 'reversion' - or the present value of all the future cashflows after the next review

A. THE PV OF THE CONTRACT RENT UNTIL THE NEXT RENT REVIEW:

The present value of the contract rent until the next review date is a simple annuity. There are advantages to minimising the number of variables in a formula when dealing with spreadsheets, not the least of which is making them easier to understand. In Excel, the value of fixed annuities is calculated with the PV formula:

Present value of income stream = PV (Rate, Periods, - Payments Future Value, Timing)

Rate is the effective discount rate per period. *Periods* is the number of payments. *Payments* is the actual rent payment per period. *Future value* is the reversionary value of the property at the end of the payments. *Timing* is equal to '1' for payments at the start of the period and '0' for payments in arrears. For property A, the present value (PV) of the contract rent until the next review period is therefore calculated by Formula 1:

That is the easy part. Note that it has been assumed that the reversionary value equals zero at this point. The owner of a perpetually renewable lessor's interest can never assume to receive the land back, but only the future income from that land. The reversionary value represents all of the future income after Year 7, when the rent is next reviewed to market. It is this calculation which requires a little bit more thinking.

B. CALCULATION OF THE REVERSIONARY VALUE

Property A:
Perpetual Lease

Previously published articles have presented various calculations that attempt to estimate the reversionary value based upon a number of inputs. This model merely applies a long term growth rate to continue the forecast of income beyond the first review date. In this instance a growth rate of 3% has been used. The forecast market ground rent payments at year 7 for property A will then be shown by Formula 2.

This payment is made quarterly for the next 21 years. This set of payments can be called the 'first review period'. The value of the total income from the first review period on the first day of that period will be another simple annuity commencing at the beginning of year 8 with payments of \$21,522.79 per quarter discounted at 10.5% per annum. The formula for valuing such an annuity is shown as Formula 3.

FORMULA I

Effective quarterly discount rate	No. of periods until review: 7 years x 4 payments per annum	Quarterly ground rent payment: \$15,000 4 payments per annum
--------------------------------------	---	--

$$\text{PV of Contract Rent} = \text{PV}((1+.105)^{(1/4)-177*4,-15000/4,011))$$

No reversionary value (at this stage)	<u>F1</u> (pa yments in advance = payments in arrears)
_ \$76,495	<u>0=</u>

FORMULA 2

Current land value	Long term growth rate:	No. years to review: 7 years	Ground rental rate: 7%
-----------------------	------------------------------	---------------------------------------	------------------------------

Ground rent payments at next review date	= 1000000*(1+.03)^7*.07/4 = \$21,523.79	4 payments per annum
Say,	= \$21,523 per quarter	

FORMULA 3

Quarterly discount rate	21 year review periods x 4 payments per annum	Formula 2
----------------------------	--	-----------

PV of first Review period	= PV((1 +.105)A(1 /4)-1,21 *4,-1000000*(1+.03)A7*.07/4,0,1) = \$765,793
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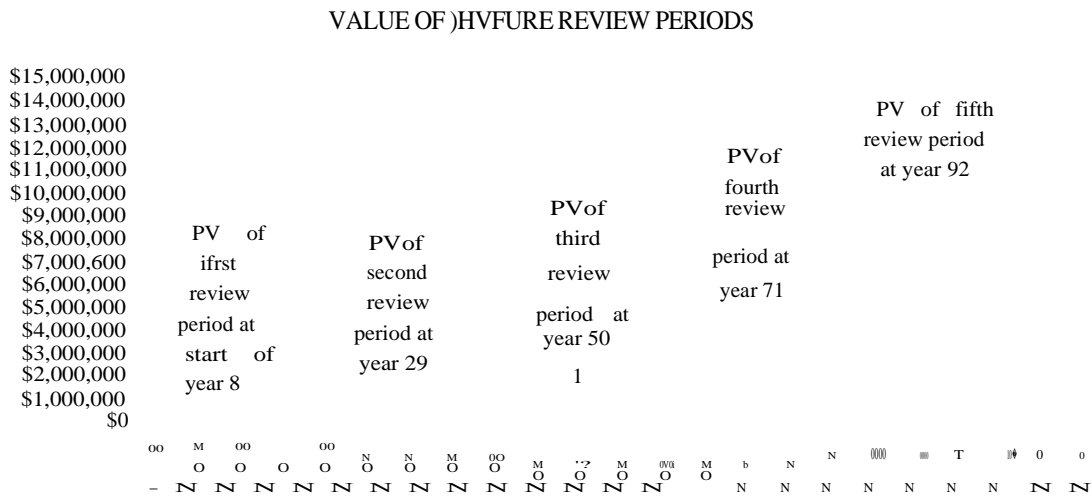
This is the value of the income from of the second review period and and then the present as illustrated
the first review period, at the start third review periods, and so on, in table 2
of year 8 (i.e. it has 7 full years to can be forecast and discounted
run until it is reviewed). The value back to their commencement dates,

Table 2

Review Periods:	First Review Period	Second Review Period	Third Review Period	Fourth Review Period	Fifth Review Period
Years to review	7 yrs	28 yrs	49 yrs	70 yrs	91 yrs
Rent per payment	\$21,523	\$40,039	\$74,484	\$138,562	\$257,766
PV of 21 years' rent at review date	\$765,793	\$1,424,600	\$2,650,176	\$4,930,109	\$9,171,454
PV to Year 0	\$380,693	\$87,006	\$19,885	\$4,545	\$1,039

If graphed, the values on the third line of this table ('PV of 21 years' rent at review date') would look like Graph 2 (continuing into perpetuity).

Graph 2



These sets of future income are an annuity inflating at a compounding growth rate. Together, they are an estimate of all of the future income after the next review date, or what has come to be known as the reversionary value of a lessor's interest.

For calculation purposes, the payments that go into the PV formula are now simply the review period values. An inflating annuity is not difficult to calculate, the discount rate is simply adjusted for growth, to produce a capitalisation rate. The growth adjusted discount

rate when payments are in arrears is given by $1 + \frac{\text{discount rate}}{1 + \text{growth rate}}$ over the whole period, divided by $1 + \text{growth rate}$ over the whole period, 1. With simplification, the growth-adjusted discount rate for this inflating annuity is shown by Formula 4:

FORMULA 4

	Annual discount rate 10.5%	Long term growth rate 3%	21 yearly rent reviews
Discount Rate for Inflating Review Periods	$= ((1+.105)/(1+.03))^{A21-1}$ $= 3.3754842 \text{ (337.54842\% per 21 yr period)}$		

Formula 3 calculated the starting payment of the inflating annuity which is the reversionary interest. Formula 4 calculates the discount rate for this series of 21 yearly cashflows implying 3% pa compounding growth, a 10.5% discount rate, and 21 year review periods. The number of these review periods of income is simply the term to final expiry, less the term to the next review, divided by the review term. In the case of perpetually renewable leases such as Property A, there are an

infinite number of review periods. The PV of the annuity with payments of \$765,792.80 can therefore be calculated by capitalising the value of the first review period by 337.54842%, and adding one payment of \$765,792.80 (i.e. as this is an annuity with payments in advance), or the following simplifies Excel formula:
While this is the simplest method of calculating the reversion, it is not flexible enough to accommodate terminating leases

without modification, and it is desirable for the formula to be able to accommodate terminating leases at times. For perpetually renewable lessor's interests it is possible to use the PV formula and assume there are, say, 100 terms of 21 year each until expiry. Any more than about 13 payments of 21 yrs each becomes irrelevant in the discounting process (i.e. an annuity lasting 2,100 years is no more valuable than one lasting 273 years).

FORMULA 5
(FOR PERPETUAL LLA F)

PV of first year review period at year 8	Growth-adjusted discount rate for 21 yearly payments with 10/5% pa discount rate and 3% growth
<p>PV of reversion (at start of year 7) = \$765,793*(1+1/3.3754842)</p> <p>= \$992,662</p>	

The single cell Excel PV formula of the reversionary income for a perpetually renewable lease can therefore be given by the following alternative version of Formula 5:

FMU!A 5
(or. r.itpfili I;al Lease)

Formula 4	No. of review periods until expiry (21 yrs x 100 approximates a perpetuity)	Formula 3	Assume no reversion as freehold land for this perpetually renewable
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$$=PV(((1 +.105)/(1 +.03))^{21-1}, 100, PV(((1 +.105)^{(1/4)-1}, 21 *4, 1000000 * (1 +.03)^{7*0.07/4}, 0, 1), 0, 1))$$

Y

t

1:Reversionary value is an annuity with payments in advance

FORMULA 6
(Perpetually Renewable Lease)

Formula 1	Formula 5 Perpetually Renewable Lease...
-----------	---

I

$$= PV(((1 +.105)^{(1/4)-1} * 4 - 1) * 5000/4, -PV(((1 +.105)/(1 +.03))^{21-1}, 100, PV(((1 +.105)^{(1/4)-1}, 21 *4, 1000000 * (1 +.03)^{7*0.07/4}, 0, 1), 0, 1), 1))$$

...Formula 5 (Continued)
Perpetually Renewable Lease

Indicated Value of Property A = \$569,970

**Property B:
Terminating Lease**

The introduction of a terminating lease does not alter the formula significantly, but the reversionary value will then be made up of two parts:

An inflating series of cashflows, i.e. the reversionary interest in income.
The reversionary interest in the land, i.e. the freehold land value.

Property B is used in this example. The market rental rate which has

been chosen for the terminating lease is 6.5% of the land value. Formula 5 will require the actual term to run (expressed in review periods) until final lease expiry in order to calculate the number of review periods remaining. In this case the number of full review periods remaining is 3 (i.e. 70 years to run less 7 years to review equals 63 years, divided by the 21 year review periods, equals 3). The PV of the reversionary interest in the freehold land value must be added into Formula 5, the annuity of future review periods. Note that the future value in the

PV formula was assumed to be zero in Formula 5. For terminating leases this future value is equal to the inflated land value. The discount rate used for Formula 5 was calculated as 337.5% for every 21 yearly payment, which assumed growth of 3% pa and a discount rate of 10.5% pa. Since the discount rate for Formula 5 already reflects growth, it is only necessary to inflate the freehold land value reversion to the start of that annuity, i.e. at the start of year 8. The freehold land value at the start of year 8 is shown as:

FORMULA 7

Freehold Land Value at present Land Value growth rate is 13% pa

$$\begin{aligned} \text{PV of Reversionary Interest in Land} &= 1000000 \cdot (1 + 0.03)^{A7} \\ &= \$1,229,874 \end{aligned}$$

7 full years of growth until start of year 8
'41-7

Adding this as the reversionary interest in land into Formula 5 gives the total reversionary interest in property B at the start of year 8;

Formula 4 No. of review periods until final expiry: 70 years to expiry 7 years to run _ 21 year terms Formula 3 revised with 6.5% ground rental rate

$$\begin{aligned} &= \text{PV}(((1 + 0.105)(1 + 0.03))^{A21-1}, (70-7)121, \text{PV}((1 + 0.105)^{(1/4-1,21)} * 4, 1000000 * (1 + 0.03)^{7.065/4, 1}) \\ &- 1000000 \cdot (1 + 0.03)^{A7, 1}) \end{aligned}$$

Formula 7

Reversionary value is an annuity with payments in advance, so timing is 1

$$= \$925,436$$

**FORMULA 5
(Terminating loost**

Incorporating this into Formula 1 gives the value of the terminating leasehold interest in property B at the start of year 8:

Formula 1

Formula 5

(Terminating lease...)

I

$$=PV((1+.105)^{(1/4)}-1)^{-4} \cdot 177 \cdot 4^{-1} \cdot 5000/4, -PV(((1+.105)/(1+.03))^{A21-1}, (70-7)/21, PV((1+.105)^{(1/4)}-1, 21 \cdot 4, 1000000 \cdot (1+.03)^{A7} \cdot .065/4, 0, 1), -10000070 \cdot (1+.03)^{A7}, 1, 1)$$

...Formula 5

(Terminating lease) coninued.

= \$536,551

FORMULA 6

$(1+i)^t - 1$ $(1+i)^t - 1$ $(1+i)^t - 1$

This terminating formula can be used in place of the perpetually renewable formula as long as the term to final expiry is greater than about 300 years, at which point the PV of the reversionary interest in land is usually discounted so heavily that it is worth less than a cent.

SIMPLIFICATION OF THE FORMULA

Having set up the formula on the basis of terminating and perpetual leases, the task remains to make it flexible and able to accommodate the many permutations of lease terms and values. The various

components of the formula can be assigned 'named' cells in the worksheet in a single-case scenario, or referenced to columns in a table containing a portfolio. For this example the named cells option has been shown, however it is not difficult to substitute cell references for the names if required.

A short cut to name cells in Excel is to type the name over the cell reference (A1, B2, C53, etc ...) in the space at the top left hand side of the screen known as the 'name box'. Seagar & Partners' formula uses the following named cells:

dr	Discount rate per annum
np	Payments per annum
cr	Contract rent per annum
rp	Review period in years
gr	Cumulative annual growth rate
t	Timing of payments: 1 = in advance, 0 = in arrears
Iv	Land value
gp	Ground rental rate (as a percentage)
ye	Years to final expiry (use 1,000 if a perpetual lease)
tr	Term to review (in years)

With this information, it is possible to calculate the lessor's interest all in one cell containing the following formula:

SEAGAR AND PARTNERS' LESSOR'S INTEREST FORMULA

$$=PV((1+dr)^{(1/np)-1, tr*np, -cr/np}; PV(((1+dr)/(1+gr))^{rp-1, (ye-tr)/rp}, PV((1+dr)^{(1/np)-1, rp*np, lv*(1+gr)^{tr*gp/np, 0, t}, -lv*(1+gr)^{tr, 1}, t))$$

PROBLEMS WITH THE FORMULA

As with any theory there will always be pitfalls and specific reasons why the formula does not ring true. These should be kept in mind when using such a formula. The mathematical difficulties are:

- There is no allowance for a ratchet clause. It would be difficult to incorporate this into the formula without adding significantly to the length. If required, a ratchet clause can be incorporated into a table such as Table 2. This is only an issue where there is current over-renting, an unusual (but not unknown) situation with ground leases.
- The Termination date is assumed to coincide with the end of a review period. This may not necessarily be the case, however unless the termination date is in the near term, the difference is likely to be immaterial.
- The model assumes standard lease terms and that a rent is fixed over the whole review term. This is not always the case, and adjustments must be made sometimes by taking the present value of the shortfall/overage in the rent until the next rental 'step' or adding in shorter terms at the end of the lease. For example, a number of Auckland City Council leases have irregular terms just prior to expiry, alternating 10 and 11 year rent review periods, or stepped rents for the first 21 years.
- The model assumes that the ground rent reviews will always be to the same percentage of land value. This is simplistic, however as with many financial indicators, the best estimate is often likely to be current data. Changes in underlying financial indicators will always affect the future expectations of income from any investment, and hence values change. If ground rental rates do change significantly, the original valuation was not wrong as it was based upon expectations at that time. New market prices will be formed from new information and altered expectations. The growth rate is assumed to be log-linear, whilst in

reality growth rates are generally cyclical, and may exhibit a near-linear long term trend line. The long term error is unlikely to be significant. If the short term growth forecast differs from the long term outlook, the short term growth rate may be used in Formula 2 to estimate growth until the next review. In this case, the longterm growth rate would be used in Formula 4 to estimate the reversionary interest in income and/or land value.

USING THE FORMULA

A. Sales Analysis

Careful sales analysis is important. Sales can be analysed to estimate discount rates. An appropriate method is to search all of the titles and leases so you are sure of all of the facts and therefore are restricted to only three judgement calls: (i) expected growth rate; (ii) freehold land values; and (iii) the appropriate ground rental rates. Consistency is important in making these estimates, however there will always be judgements required. Many portfolios have been the subject of periodic revisions by a valuer who may be able to assist in providing previous land value estimates for sales analysis. The aim of the sales analysis is to calculate the Discount rate that makes the Lessor's interest equal to the sale price. This is the expected Internal Rate of Return (IRR) to the purchaser. Excel has a Goal Seek function which can be used for this calculation.

B. Portfolios

When dealing with more than two

lessor's interests, it is advisable to set up a spreadsheet with a line for each property. Each line contains the variables such as land value, term to review, perpetual or terminating lease, payment frequency, review period, market ground rental percentage, payments in advance or arrears, and contract rent. The main operators, the growth and discount rate cells, can remain named and form part of a summary table which adds all the individual lessor's interests calculated on these single assumptions to an overall value for the portfolio.

C. Growth Rates

This is an area in which would benefit from further research. It would be unwise to rely on historic growth rates over the last 30 years, as these may well not be realistic in a low inflation environment. There is always the danger that the growth will be over-estimated. The writer believes that compounding annual growth rates of 2% to 5% are conservatively realistic at present for CBD commercial properties. Forecast growth rates should take into account analysed historical real growth rates and forecast nominal inflation.

A perfect model would incorporate cyclical land value and yield movement, however to do this would require a sound rationale in order to be convincing. Having said this, it would not be unreasonable to assume different growth rates in Formula 2 and Formula 4 for short and long term growth. Table 2

illustrates that the largest value component is usually the first review period, and so an over-estimation of later future returns may be insignificant when weighed up against the more realistic estimate of the first review period income.

Adjusting growth rates between properties would be difficult, as the market's expectation of abnormal future growth should be already included in the estimated market freehold land value. Locational disparities in growth rates over the past are not necessarily any indication that this will happen in the future, and in fact may be an indication values have caught up to the surrounding locations and thereafter growth will be consistent. Having said this, there are likely to be certain cases in which it is quite appropriate to make an adjustment to the growth rate.

If the assumptions are consistent, the discount rates (IRR's) analysed from sales would be expected to be relatively consistent. If the growth rate has been overestimated the discount rate will be slightly higher than expected, and likewise with the land values. Whilst this could lead to errors, the discount rate is affected, so if consistent discount rates, growth rates, and land values are used in both sales analysis and valuations then the errors will largely cancel each other out.

Our sales analyses of discount rates appear to correlate well, however this is likely to be

because the model is similar to that used by advisers to other market participants. Further empirical research utilising market indices is necessary for the establishment of a factual basis for arguing discount rates and growth rates.

CONCLUSION

The above formula sets out a basis of calculation of lessor's interest values, but it is simply a discounted cashflow calculation. The writer hopes that it is useful to other valuers, and also that it brings some consistency to the way we, as a profession, deal with such properties.

*Reid Quinlan
BPA Diploma in Business
(Finance) Registered Valuer,
ANZIV*

Reid Quinlan has been with Seagar and Partners since early 1994. A significant portion of his time over the last several years has been devoted to valuation of leasehold portfolios, together with typical CBD valuation assessment. This model was developed while he was completing a Diploma in Business (Finance) from Auckland University in 1996-97.

Valuers and Contaminated Land: *Approaches Used in New Zealand Practice*

Sandy G. Bond
Paul J. Kennedy

Abstract:

Increasing litigation involving land contamination and an escalation in the number of incidents where property owners have suffered financial losses from such cases has resulted in negative impacts on property values and greater risks associated with investments in contaminated property. Yet it appears that valuers themselves are uncertain as to the correct approach to take, to account for these risks in their valuations.

To help determine a set of "best practice" approaches which valuers can use when offering

advice and producing valuations of contaminated land the identification of the current methods and approaches adopted is needed.

This paper summarises the results of research undertaken within New Zealand, building on the work done in the UK by Kennedy (1997), to answer the question of how those who are involved in offering advice and valuing contaminated property evaluate its affects and incorporate this into such calculations and advice. This study is to be used to help develop specific industry guidelines on the procedures and methods to adopt when valuing such property.

1. BACKGROUND: THE VALUATION OF CONTAMINATED LAND IN NEW ZEALAND

It was the introduction of the Resource Management Act (RMA) in 1991 that brought contaminated land issues to the attention of valuers, and highlighted the need for them to take this into account in calculations of worth. However,

uncertainty exists as to the effect contamination will have on property values due mainly to a paucity of contaminated property sales together with the lack of clarity within the legislation over legal liability for polluting.

The RMA presently only goes so far as allowing local authorities through the Planning Tribunal to issue enforcement orders and abatement notices to owners

(either current or previous) or occupiers of contaminated sites, or to those that caused the adverse effect on the environment (the polluter), requiring them to remedy this. There is no formal hierarchy of liability between these parties and any one, or all, are potentially liable (similar to the US "Superfund" approach). Alternatively, the local authority has the power to clean up the sites themselves and seek to recover the costs from the liable parties.

Bond et al. (1997, p2) outline the areas where the legislation may be unclear and a source of confusion for valuers. These include: who is responsible for the contamination; who is to pay for the risk assessment and clean-up costs; who is responsible for "orphan" sites; who is responsible for selecting appropriate remedial solutions; who will determine the degree of remediation required; and will liabilities be retrospective. Resultant perceived financial risks may have a substantial effect on assessments of property value.

Coupled with these uncertainties is, firstly, the difficulty in identifying if contamination exists on a site, and secondly, the specialized skills required to determine the extent of contamination and the costs of remedying it once it has been identified. These are the problems that the valuation profession has had to face when valuing property known or suspected to be contaminated.

While it is recognized that valuers do not have the requisite skills to undertake environmental audits or extensive site investigations to determine the presence and extent of site contamination it is not appropriate that they simply decline instructions to value property where contamination may be an issue. However, uncertainty exists over the correct approaches to take and methods to use when valuing property affected by contamination to avoid the risk of legal liability.

The objective of this research is to identify the approaches used by valuers in NZ when offering advice and producing valuations of contaminated land. Similar studies in the UK completed by Paul Kennedy and Tim Richards in 1995 and 1997 revealed some interesting results. These studies considered together can be used to help develop specific industry guidelines internationally on the procedures and methods to adopt when valuing such property.

2. BRIEF LITERATURE REVIEW

Bond, et. al. (1997) provides a comparison of attitudes and policies of investors and lenders in NZ and the US toward investing in and lending on property known or alleged to be contaminated in 1996/97. This indicated that both debt financing and equity investment funds are available for the acquisition and ownership of properties affected by contamination, but more particularly in the US than in NZ. Exceptions to this included properties with on-site

radioactive waste or radioactive handling materials and properties in close proximity to such facilities. While NZ has had the opportunity to benefit from the experiences of the US with regard to site contamination, many issues surrounding these, particularly those relating to clean-up liability, are still uncertain. Thus, the differences in responses between the two countries was not surprising.

This research provided a good background and focus for the current research to help determine whether the caution evidenced in that study is taken into account by valuers in practice and how they go about incorporating the risks associated with contaminated land into their value calculations.

Joyce and Parker (1994), and Hemmings (1994) highlight the responsibilities of valuers involved with valuing land known, alleged, or suspected to be contaminated and provide guidance on the factors to consider, and the due diligence approaches to take, to avoid the potential liability arising from such.

Harding (1994) explains the potential liability under the RMA placed on bankers and lenders in NZ, and the role that valuers can play in reporting potential problems. He outlines the approach valuers should take when valuing property that may be affected by contamination as reported in the International Asset Valuation Standards Committee Information Paper No.

11: "Effect of Environmental Factors and pollution ". This states:

"2. Where a problem is identified by normal diligence, it is the Valuer's responsibility to provide a valuation in which the nature, extent and result of inquiry must be disclosed, whether based on the Valuer's research or an external environmental audit. "

"2.3 Where any such pollution is not within the experience and competence of the Valuer, the client should be advised to obtain technical advice. The completion of the valuation would then require association with or the retention of others who possess the required knowledge and experience, "p. 13.

Drawing on information from both the UK and US Dixon (1995) found that most valuers adopt a 'cost to correct approach' to the valuation of sites affected by contamination. Typically, the cost to correct approach entailed the deduction of estimated remedial costs from an assessment of the 'clean' value of the site. Richards (1995) after surveying valuers in England and Wales came to similar conclusions. As highlighted by Kennedy (1997) these approaches tend to ignore the impact of contamination on revenues, the distribution of costs over time and perceived financial risks ("environmental stigma").

While the use of a value adjustment for environmental stigma is advocated by a number of commentators including Mundy (1992), Syms (1996) and

Richards (1997), only a few of the valuers surveyed by Dixon (1995) and Richards (1995) use one. However, their adjustments tend to be subjective (a yield or capital value adjustment).

Syms (1996) criticises the subjectivity of a yield adjustment based approach for reflecting environmental stigma. As a solution he provides an alternative methodology. He proposes a model that attempts to identify factors influencing potential purchaser's perceptions of financial risks generated by contamination. Using this information the scale of the required value adjustment to reflect environmental stigma is quantified. Value assessments produced using this model have yet to be tested for reliability and accuracy. In addition, quantitative requirements of the approach may limit its perceived pragmatism.

Through surveys of UK valuers Kennedy (1997) identifies a wide range of investment valuation methods used in practice for sites affected by contamination. Although a number are similar the majority have idiosyncratic details. Analysis conducted shows that these variations have a substantial effect on assessments of value.

2.1 Professional Guidance

In the UK guidance from the RICS on the valuation of contaminated land has avoided detailing suggested methodologies (RICS, 1995). Instead guidance has been restricted to information on the range of potential value effects

and the characteristics of contamination and remediation. Kennedy (1997) suggests that this approach may have caused methodological inconsistencies in UK practice.

The Australian Institute of Valuers and Land Economists (AIVLE) Contaminated Land Practice Standard (1994) outlines the types of contamination that exist, and their impact on value, then recommends to its members the use of four main valuation approaches to the assessment of property affected by contamination, as appropriate, as follows:

- (i) Unaffected Valuation basis - where it is assumed, after preliminary investigations, that the land is not contaminated;
- (ii) Affected Valuation Basis the discounted value after taking account of the costs to remedy the contamination;
- (iii) Environmental Balance Sheet Approach - the unaffected value less all costs associated with remedying the contamination: site investigations; clean-up; liabilities; remediation management; and stigma (if any),
- (iv) Comparative Approach use of comparable evidence to assess both the unaffected and affected property value.

The New Zealand Institute of Valuers has published similar guidance notes for its members: *Guidance Note 3: Valuation of Contaminated Land and Bibliography* (1995). These were

adapted from *The Royal Institution of Chartered Surveyors' Valuation Guidance Note 11* (1993, now revised). It outlines a number of factors that the valuer should take into account when valuing property affected by contamination and suggests a "before and after" valuation approach where the property is valued "before" as if no contamination occurred and the "after" once all costs associated with remediation, including the effect of stigma and other risks and uncertainties, have been deducted.

Despite these above mentioned guidelines and suggestions it appears from the literature that valuers in the UK remain unclear on the methodology to adopt when valuing contaminated property. The research presented in this paper indicates that this uncertainty also exists amongst valuers in NZ. It is suggested that these weaknesses may be addressed through the development of a set of 'best practice' valuation methodologies. This paper represents a contribution to this objective.

3. SURVEY OF NZ PRACTICE: THE VALUATION OF CONTAMINATED PROPERTY

3.4 Objectives of the Survey
This research was undertaken in New Zealand in 1997/1998 to identify the approaches used by valuers when providing advice or producing valuations to account for the financial risks associated

with investing in contaminated properties. The results will subsequently be compared with those from similar studies conducted in the UK and US' to help ascertain a set of "best practice" approaches.

3.2 The Research Procedure
Although there is potential for all valuers to be faced with valuing land affected by contamination it is likely only a fraction of these will become involved in such work. The latter experienced "sub-group" are more likely to respond to a survey investigating valuation methods for valuing sites affected by contamination. Given the large number of valuers in the NZ (2026 members of the NZ Institute of Valuers at December 1997, 1004 of these hold practicing certificates) a targeted approach was considered most appropriate, rather than surveying all valuers.

To identify those involved in valuing land affected by contamination, and those with an interest in such, a Call for Participation was included in the *New Zealand Valuers' Journal* which was mailed out to all valuers in NZ in December 1997. To enhance the validity of comparative findings between this study and the Kennedy (1997) study, a similar survey instrument was used to that adopted by Kennedy.

UK: Paul Kennedy conducted a survey of UK practice in the investment valuation of sites affected by land contamination as part of his Ph.D. studies (completed in 1997); US: Dr.'s Elaine Worzala & William Kinnard Jr, are about to commence research to find out how appraisers in the US value contaminated property.

Kennedy's carefully developed and pre-tested questionnaire achieved an overall response rate of 54% after two follow-up reminders. However, the results of a pilot study of five valuers in NZ (and the two academics who are to undertake the US-based survey) indicated some modifications were required to simplify and shorten the eighteen page UK survey instrument, as well as to adapt it for NZ (see section 3.3 for details).

The resulting ten page questionnaire was divided into two parts: the first Part A included questions to determine the respondents professional and personal background, while the second part addressed valuation techniques. This latter Part B was divided into three sections. The first section asked questions to determine the valuers level of experience with valuing contaminated property, how they identify contamination, and once identified, their approach to the valuation task. The second section sought information about the valuation approaches adopted to value contaminated property while section three (divided into three parts) included questions to provide information on the approach respondents take to each valuation variable² (i.e., its quantification and integration into calculations of value) and the sources of information used to determine these.

Once the US study is complete all three countries results (US, UK, NZ) will be compared to help assist in developing industry

guidelines internationally on the procedures to adopt when valuing property affected by land contamination.

3.3 Pilot Survey Results

Five valuers were identified and selected on the basis of either their standing within the profession or their interest or involvement in the valuation of contaminated land. Selection was also aimed at providing a balance of views from valuers employed in either private practice or by the government.

Generally, it was agreed that the UK survey instrument was too long and detailed, and that both the profit approach and residual methods were not particularly relevant in the NZ context. Further, it was felt that there was no need to differentiate between "market value" and "investment value" assessments.

Two interviewees warned of the shortage of valuers involved in the valuation of contaminated land which could adversely affect

the survey response rates and results. For this reason, a targeted approach to respondent selection was suggested, in the form of an invitation to be involved in the survey. Another felt that the one year time frame used to question how many valuations had been undertaken of contaminated land was too short, as it was assumed that the majority of valuers in NZ undertake such work infrequently.

i.e., revenues; costs; time; and perceptions of risk and uncertainty.

One interviewee suggested that valuers do not want to get involved with this type of work at all (if the existence of contamination is already known) due to potential legal liabilities. Another suggested that valuers who do undertake this work tend to use disclaimers in their reports regarding contaminated land (rather than adjusting for it in the value estimates). One suggested, as a result of the lack of experience with contaminated land issues in New Zealand, that overseas experience is going to be more helpful and that most valuers are already looking to this as the basis for their own determinations.

It was pointed out that it is usually only when the property is sold or the use changes that contamination is noticed. Often the owner is aware that the contamination exists but does not want to make this known so may choose not to sell the property. However, despite this fear of exposure it was pointed out that sites known to be chronically contaminated may still be able to be used if the contamination is capped and contained. Thus, it was felt that the extent of contamination was not necessarily as important as the most likely use of the land. The valuation approach suggested in these cases was to simply deduct the cost of capping from the value uncontaminated (with Council Contaminated Lands Registers and LIM's providing details).

Contamination costs were highlighted as important issues that needed special focus in the

survey: what these are, and how they are estimated. These issues were also raised as a criticism of valuers in subsequent correspondence with a geo-environmental engineer, involved in the assessment and remediation of industrial sites. He voiced concerns that valuers and real estate consultants are not making allowance for the costs of remediation. He noted that "while there is a general awareness of contaminated land in NZ as a consequence of the Resource Management Act there appears to be little action taken by these professionals in establishing the costs and the determining the overall effect on property values". From his observations it appears that much of this activity is left up to the purchaser.

Interestingly, one interviewee suggested that as the costs of clean-up are often more than the value of the property, such a property cannot be valued.

It was suggested that no distinction be made between environmental risks and uncertainties but that they should be included together. One interviewee considered that an allowance for this using an increase in yields was an unlikely approach due to the lack of evidence upon which to base the quantum of the increase. Further, they suggested that cash flow reductions for monitoring costs might be a satisfactory approach, but that other cash-flow based allowances (say, for risk and uncertainty) are purely speculative.

The identification of contaminated land was highlighted as the main issue rather than the valuation of it, as well as the "more nebulous" allowance for potential contamination. To this end a question was suggested for inclusion to determine how valuers go about identifying such land (investigative measures taken). Based on all of these suggestions and responses the final questionnaire was developed.

4. Summary Of Survey Responses

4.1 Introduction

The summary of the major findings that emerged from the survey is presented in this section with accompanying Tables in Appendix A. To keep this section brief, only a limited amount of data is cited directly.

4.2 Response Rates from the Survey

The questionnaires were administered by mail in December 1997 to those who had responded to the Call for Participation. Initially, seven responses were received out of fifteen to whom surveys were mailed indicating an overall response rate of 47%. Reminder letters were sent out to the remaining 8 respondents, two of whom returned the questionnaires unanswered explaining they felt unqualified to answer it, and six whom failed to reply by mid March 1998.

4.3 Part A: Experience & Organization Type (Q's 2-3)

The questionnaire was divided into two parts: the first part

included questions to determine the respondents professional and personal background, while the second part addressed valuation techniques. Question 1 asked respondents to specify their office location. The respondents were broadly based geographically coming from as far south as Dunedin and as far north as Auckland, but with none from the main centres as expected. The breakdown of the type of respondent organization (question 2) indicates that nearly three quarters of the respondents are in private practice, with the remainder working in central or local government.

4.4 Part B: The Valuation of Contaminated Land

4.4.1 Section One: Experience with Contaminated Land (Q's 4-5)

As the main purpose of adopting a targeted approach to respondent selection was to attract respondents with experience in the valuation of contaminated land it was expected that they would have had at least some experience in this work. This was confirmed by responses to the question regarding the number of valuations undertaken in the last five years of property where contaminated land was an issue. All respondents had carried out at least 1-25 valuations in that period.

The question also asked respondents to specify the types of contaminated properties on which they have provided valuation advice. They indicated

a number of land uses including: a tannery site (14.3%); former landfill site (14.3%); timber treatment sites (57%) with only one not specifying their involvement.

The majority of the valuations conducted by respondents had been of industrial properties, with one respondent also having been involved with valuing rural property affected by contamination.

4.4.2 Reactions To Contaminated Land Valuations (Q's 6-8)

Question 6 asked respondents to identify the action they take when they have positively identified that contamination exists on a property they are valuing. Nearly three quarters of the respondents value the property as if uncontaminated, and include a disclaimer, with 60% of these also responding that they would value the property as contaminated if costs to remediate the contamination were available. One respondent (14.3%) said that the choice of approach would depend on the client's instruction. The remaining respondents (28.5%) would value the property as if contaminated from the outset. None of the respondents would decline accepting the valuation job.

Respondents were then asked what investigative measures they take to determine the presence of contaminants. All respondents employed varying combinations of the response options: view City Council register of contaminated properties; a Land Information

Memorandum; monitoring reports from the owner/occupier and obtain engineering reports as a precondition to making a valuation. Other investigative measures respondents listed were: District Council Hazard registers and property files, and Regional Council reports. One respondent indicated that they usually have to resort to their own analysis. Presumably each measure sought would depend on the nature of the valuation project.

These investigative measures were exercised by 85.7% of respondents only on properties suspected to be contaminated, with 14.3% undertaking them on all properties valued. This would tend to reflect how thorough and cautious valuers are with those undertaking such procedures on all properties valued showing greater due diligence than those that do not take such precautionary measures. These results are of concern given that it is usually only after making these investigations that contamination is discovered.

4.4.3 Section Two: Valuation Approaches and Contaminated Land (O's 9-10)
To help avoid misunderstandings definitions of the various approaches discussed in the questionnaire were presented prior to the questions relating to these.

Question 9 addressed the frequency each valuation method was (sales comparison and income) in the last five years. Over half (57%) of the respondents use both approaches 75-100% of the time, 28.6% do not

use the sales comparison approach at all, and 14.3% do not use the income approach.

These results indicate that while the sales comparison approach is used by many, the income approach is the preferred method to value property affected by contamination. All respondents indicated use of more than one method of valuation. This may be interpreted in two ways: methods employed may differ according to site type; or some respondents may use more than one method for a single calculation. Such a combined approach is common in US texts, and recommended practice in NZ.

Question 10 asked what the percentage of the Income Approach used to value contaminated property investments in the last 5 years have been presented as full DCF calculations (as opposed to a short-cut DCF). Nearly three-quarters of the respondents do not use full DCF at all, and the remaining respondents (29%) only use it 5-25% of the time. This confirms the expectation that less sophisticated income based methods are used in these valuations. Given the simplistic nature of the short-cut DCF (or direct capitalization) method this finding maybe of some concern, particularly when regarding the complexity of contaminated property valuation.

4.4.4 Section Three: Valuation Variables

(i) Part One: Net Ordinary Income (O's 11-14)
Section three investigates respondents approaches to valuation variables: income;

contamination costs and environmental risks and uncertainties. Questions 11 to 14 deal with net ordinary income. The first question asks about information sources commonly used to base the quantification of initial net ordinary income and its rate of growth over the investment life of a contaminated property. Results indicate that respondents base their assessments on more than one source of information.

Over half of the respondents use their experience and all of them use comparable evidence from uncontaminated properties similar in location to the subject property. In combination with experience, 43% use this as their sole evidence. Many, (71%), justify using it on the basis of a lack of directly comparable contaminated property sales evidence. Nearly a third responded that they would use all of the comparable evidence options available. Market forecasts and economic data were used by 43% of respondents to aid their assessments. These results highlight the difficulty in finding comparable evidence of contaminated properties and the need to use whatever other comparable evidence is available.

Question 12 asked how respondents incorporate estimated rate(s) of future net ordinary income growth (and/or decline) over the life of the contaminated property investment into the valuation. Over half of the respondents increase or decrease the yield or discount rate (reflecting and confirming the use

of the short-cut DCF approach), 14.3% use an increase or decrease of net ordinary income estimates, and a similar percentage make use of both approaches (with the explanation that the approach used depends on the circumstances). One respondent (14.3%) failed to respond.

Question 13 asked what, if any, temporary interruptions to net ordinary income respondents have experienced that occur as a result of land contamination. Site investigations were the most commonly identified interruption to income (57%), remediation works were the next, with site monitoring and legal actions the least frequently identified options. One respondent listed the requirements of the Occupational Safety and Health (OSH) Council requirements posing possible interruptions (and costs). Two of the respondents (29%) did not indicate any experience with interruptions to income.

Question 14 considered approaches to the adjustment of market values to reflect voids in revenues (e.g. for remedial requirements). Over 40% of respondents make an explicit reduction or termination of the revenue for the specified period (i.e. alter the cash flow). Over half (57.2%) of the respondents increase the yield (the more traditional and simplistic approach). Nearly a third of the respondents (28.6%) failed to respond.

The responses to Question 14 were surprising. Given that 42.9%

of the respondents reduce or terminate the net ordinary income for specified periods and that this approach has similarities to a full DCF approach, the response tends to conflict with the results from question 10 which indicated full DCF analysis was not used. One explanation for this might be that respondents use a variation of the short-cut DCF that has attributes of a full DCF approach.

(ii) Part Two: Contamination Costs (Q's 15-17)

Question 15 considered information sources used to assess likely contamination costs. All respondents indicated use of more than one source of information. Nearly a third of respondents rely upon their own experience for assessing contamination costs, but in combination with other information sources. All respondents used information provided by site investigations of the subject property, specifically the cost remediation strategy, with a Phase II site assessment been the second most favored site investigation information source (71% selected this option), 57% use Phase I reports, and least favoured was use desk studies (29%).

Question 15 also considered potential for using comparable evidence to quantify contamination costs. Less than half (43%) indicate potential for the use of comparable data in the assessment of remedial costs (i.e., the quantification of costs for the remediation of the subject site based upon information on costs incurred at comparable sites). All of these respondents use contaminated

properties similar in type(s) of contamination but not location. Two thirds also use contaminated properties similar in both location and type(s) of contamination, with the other third also using uncontaminated properties similar in location to the subject property and contaminated properties similar in location but not type(s) of contamination. These results are of some concern given that remedial costs are primarily site specific, determined by the nature of the site and associated contamination. However, as these respondents use such information in conjunction with the other site investigation sources, the concerns are lessened.

Overall the results to question 15 are reassuring as they suggest that valuers are using reliable sources of information in their assessment of contamination costs.

Question 16 asked how respondents incorporate estimates of contamination costs into their valuations. Only 42.3% of respondents use a cash flow adjustment. Over a half (57%) of the respondents deduct the present value of anticipated costs. More predictably, the majority (57%) use a capital deduction (of the total value not the present value). The popularity of this simplistic approach should represent a source of concern as it is likely to produce a lower value than if the present value of those costs were deducted.

It is heartening, at least, that none of the respondents use the simplistic approach of using a discount or yield rate to adjust for

contamination costs. Further, the results indicate at least limited use of an approach which has similarities to a full DCF approach. However, this tends to again conflict with the results from Question 10 which indicated full DCF was not used. Finally, 43% of respondents use more than one approach to adjust for contamination costs.

Question 17 asked if the approach to incorporating these cost assessments into valuations changed for each type of contamination cost. Over two thirds of the respondents replied in the negative and 29% in the positive. This indicates that the majority of respondents do not adopt an analytical approach by distinguishing between characteristics of different cost types and their impact on value.

(iii) Part Three:
Environmental Risk and
Uncertainty(Q's 18-19)

The remaining questions examine risks and uncertainties caused by land contamination. Question 18 asked on which information sources respondents base their assessment of environmental risks and uncertainties attached to cash flow estimates for a contaminated property.

Half of the respondents answering Question 18 typically use comparable evidence from uncontaminated sites in similar locations to the subject property to quantify the value adjustment required for perceived financial risks. However, it is unclear what useful information may be

obtained from transactions where contamination was not an issue. Half of respondents use evidence from contaminated sites similar in location but not type(s) of contamination to the subject. Over 80% of respondents use evidence from sites similar in contamination type but not location with the same percentage (83.3%) also using evidence from sites similar in both location and type of contamination. As stated above the availability of such data is likely to be restricted. Only 17% of the respondents specified use of a form of cash flow risk analysis. This may reflect limitations in the quantitative complexity of valuation methods used by the majority of respondents. Alarming, two thirds of the respondents also used their own experience, but this was countered by the use of this source in conjunction with the other sources specified. Typically, information limitations were used to justify the use of simplistic approaches.

Question 19 asked how respondents incorporate estimates of environmental risks and uncertainties into their valuations. As in previous questions, respondents were allowed to indicate more than one method. Of those that responded to this question (86%), half used more than one method. The majority of those responding (83%) use a yield or discount rate adjustment, with a third of these using it as their sole technique. All of those that used more than one technique used this latter technique in conjunction with a

reduction in cash flow estimates.

Only 17% use a reduction in sales comparison value estimates as their sole method to adjusting for environmental risks and uncertainties. This, together with the predominance of a yield or discount rate adjustment confirms the use of simplistic approaches to valuation. However, this is tempered by the use of more than one method by at least half the respondents, who combine simplistic approaches with more sophisticated techniques.

The concluding section of the survey provided space for respondents to describe any aspect of their approach to the valuation of contaminated land not addressed in the preceding questions. The comments received, rather than adding new information, restated the approaches used and why. They value the site on an uncontaminated basis (but with a disclaimer) due to the lack of comparable evidence, and deduct (or make reference to) the costs to correct the contamination (and any other allowances for risks, uncertainties and on-going costs). One respondent noted that details of contamination are not included in the local body records which compounds the problem of information availability.

4.5 Summary

The response rate to the survey was disappointing, although not surprising, given the suspected small number of valuers in NZ with experience in valuing

contaminated property. This characteristic may limit the reliability of the results from the survey.

As well as confirming the expectation that few valuers have experience with valuing contaminated land the survey results indicate that the approaches adopted in the valuation of contaminated land are of limited complexity. Generally, respondents value the property uncontaminated and include a disclaimer, but may value it contaminated if the costs to correct this are known.

Investigative measures taken vary widely but with the majority of respondents relying on more than one source of information. For estimates of net operating income, contamination costs and environmental risks and uncertainties a reliance is placed on as many information sources as possible as there is little fully comparable information available. Net ordinary income changes (growth or decline) are predominantly incorporated into the valuation by increasing (or decreasing) yields. Similarly, estimates of environmental risks and uncertainties are most often accounted for in this way. Contamination costs are accounted for by either deducting them from the estimated value directly, or deducting the present value of the costs from value. However, as stated previously sourcing or estimating such costs is often left to other parties.

5. CONCLUSION & RECOMMENDATIONS

The survey highlights a general lack of experience with valuing contaminated properties in New Zealand and an absence of information relating to this. Many are relying on simplistic approaches to valuation partially due to the absence of comparable evidence and other necessary information. These results reflect the experience in the UK as reported by Kennedy (1997), Dixon (1995) and Richards (1995). However, unlike the UK studies, "environmental uncertainties" (sometimes known as "stigma") do appear to be accounted for in NZ, through a yield or discount rate adjustment.

From both the pilot study and the survey responses it appears that the important issues in the valuation of contaminated land are:

- how contamination can be identified,
- establishing what the likely use of the land might be once the site is remediated,
- estimating the costs of remediation to a level where the site can be used for the identified purpose.

Clearly, to resolve these issues, more information is required.

Many issues with regard to contaminated land remain unclear. For instance, until Council Contaminated Land Registers fully reflect the existence of all contaminated sites then viewing of such will not guarantee that if a site is not listed it will not be contaminated. The continued

development of publicly notified records will aid this process.

To avoid potential liability valuers should consider, rather than disclaiming responsibility (which may not hold up in a court of law), employing professional expert advice from those qualified to positively identify its existence. Such consultants are trained to determine the extent of contamination and suggest remediation strategies for identified uses and the costs involved with this. Such remediation strategies recommended should be advised in consultation with the local authority who have the power to approve or disapprove uses (via the granting of resource consents) and may also suggest or require specific remediation strategies (as a condition of resource consent approval).

Whilst this study confirms the findings from other similar overseas studies, it has, at least, highlighted the need internationally, for more specific valuation guidance, greater legislative certainty, and more publicly available data on contaminated land. Further research is warranted to help aid this process.

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Paul Kennedy joined the firm Henderson Real Estate Strategy Ltd., to head their UK research division after completing his doctorate from Nottingham Trent University in 1997. Paul maintains his connections with the University on a contract teaching basis. His doctoral dissertation thesis examines methods used for the valuation of sites affected by land contamination.

APPENDIX A: TABLES

Table 1: Background & Experience

<i>Factor</i>	<i>Frequency %</i>
<i>Q2. Type of Organisation</i>	
Private Practice	71
Central/Local Government	29
<i>Q3. Years of Experience</i>	
0-2 years	14.3
2-5 years	0
5-10 years	0
10-15 years	28.5
over 15 years	57
<i>Q4. Number of Valuation of Contaminated Properties in last 5 years</i>	
0	0
1-25	100
25-50	0
50-75	0
75-100	0
Over 100	0
<i>Q.5 Type of Property Valued</i>	
Residential	0
Commercial	0
Industrial	100
Rural	14.3
<i>Q.6 Attitude Toward Valuing Contaminated Property</i>	
Value uncontaminated + a disclaimer to this effect	28.5:83.3
Value contaminated (if costs are available)	28.5:83.3
Decline accepting the valuation	0
<i>Q.7 Investigative Measures</i>	
City Council register of contaminated properties	83.3
Land Information Memorandum	83.3
Monitoring reports from the owner/occupier	66.7
Obtain engineering reports as a precondition to an valuation	50
<i>Q.8 Are Investigative Measures Taken On:</i>	
All properties valued	14.3
Only properties suspected to be contaminated	85.7

Table.2 ♦ Valuation Approaches & Income Assessment

Q9. Percentage of Valuations Using Various Methods		
Factor	<u>Sales Comparison Approach</u>	<u>Income Approach</u>
	Frequency %	Frequency %
0%	28.6	14.3
0-25%	14.3	0
25-50%	0	14.3
50-75%	0	14.3
75-100%	57	57
Q10. Percentage of Income Approach that Comprise a Full DCF		
Factor	Frequency %	
0%	71	
5-25%	29	
25-50%	0	
50-75%	0	
over 75%	0	
Q11. Information Source or Estimate Net Ordinary Income		
Experience	57	
Uncontaminated properties similar in location to the subject	100	
Contaminated properties similar in location but not type(s) of contamination	50	
Contaminated properties similar in type(s) of contamination but not location	50	
Contaminated properties similar in both location and type(s) of contamination	33	
Available market forecasts/economic data	42.9	
Q.12 Method to Incorporate Income Changes into the Valuation		
Increase or decrease the yield rate	83.3	
Increase or decrease NOI estimates by the growth/decline rate over the life of the investment (ie at each rent review)	33.3	
<u>Other, please specify</u>	0	
Q.13 What Temporary Interruptions to Income Due to Contamination		
<u>Site investigations</u>	57	
Remediation works	42.9	
<u>Site monitoring</u>	28.6	
Legal actions	14.3	
<u>Nil Experienced</u>	42.9	
Q.14 How do You Incorporate Income voids in Valuations		
No adjustment	0	
Increase the yield or discount rate	57.2	
Reduce the sales comparison value	0	
Reduce or terminate of net <u>ordinary</u> income for <u>specified periods</u>	42.9	
<u>No Response</u>	28.6	

Table 3: Contamination Costs & Risks/ uncertainties

Factor	Frequency %
<i>Q.15. Information Source for Estimating Contamination Costs</i>	
<u>Experience</u>	28.6
<u>Desk study</u>	28.6
Phase I Environmental Audit	57
Phase II Site assessment an invasive <u>investigation</u>	71
Cost remediation <u>strategy</u>	100
Uncontaminated properties similar in location to the subject	14.3
Contaminated properties similar in location but not type(s) of contamination	14.3
Contaminated properties similar in type(s) of contamination but not location	42.9
Contaminated properties similar in both location and type(s) of contamination	28.6
<i>Q.16 How do You Incorporate Contamination Costs into the Valuation</i>	
Deduct contamination costs from NOI as they occur over the investment life	42.3
Deduct contamination costs from the estimated value	57
Deduct <i>the present value</i> (calculated using the appropriate yield) of contamination costs from the estimated value	57
Deduct the <i>annual equivalent</i> of contamination costs from net ordinary incomes over the investment life	0
Increase the yield to reflect contamination costs	0
<i>Q.17 Does Your Approach to Incorporating Costs Change for Each Type of Cost</i>	
Yes	29
No	71
<i>Q.18 Information Source for Estimating Environmental Risks & Uncertainties</i>	
<u>Experience</u>	57
Uncontaminated properties similar in location to the subject	50
Contaminated properties similar in location but not type(s) of contamination	50
Contaminated properties similar in type(s) of contamination but not location	83
Contaminated properties similar in both location and type (s) of contamination	83
Cash Flow risk <u>analysis</u>	17
<i>Q.19 How do You Incorporate Risks & Uncertainties into the Valuation</i>	
Increase the yield or discount rate	83.3
Reduce cash flow estimates	50
Reduce sales comparison value estimates	33.3

VALUATION OF NON-COMMERCIAL ASSETS

(Can heritage be valued?)

Kenneth R Taylor

This paper examines the theory and practice of valuing assets which have no direct commercial benefit. In particular the focus is on the value of cultural and natural heritage. Dialogue on this topic has spanned the last three decades and some of the literature relative to the topic is reviewed. Examples in the paper draw on experience relating to nature conservation and environmental protection particularly applicable to the mountain lands of New Zealand's South Island. The involvement of cross-cultural and cross border involvement in this "market" is a component of the analysis. The paper draws the conclusion that property valuation may have one or more components of heritage value, each of which will require different parameters for assessment.

INTRODUCTION:

The concept of valuing non-market assets has been with us for some time. It was encountered by students of resource management during the 1970's, and was by no means a new concept then. As we approach the new Millennium there is an increased emphasis in establishing quality of life for an ever growing population. There is an economic reality attached to this as Governments attempt to balance economic necessity against quality of life. Non-market valuation in this paper largely refers to those matters associated with quality of life and in particular heritage values. The paper concentrates on some events that are happening in New Zealand, but it is understood that this a world wide phenomena.

There are those that would say that valuing components of natural or cultural heritage is a myth. Molesworth (1997) said: *This is a paper which seeks to raise the question whether Western economic principles have, in recent years, subverted principles and philosophies which some might describe as "higher": higher philosophies which recognise that social order across all cultures involve a deep seated intellectual appreciation of a range of inherent values. Many of these inherent values are impossible to quantify in economic or monetary terms, but nevertheless just the institution of protected measures simply because a stable society based on age old values*

recognises the worth of keeping things which are simply dear to the heart, a place, a culture or a people.

While the sentiment is shared by many and is not a new one, the harsh reality is that Governments at all levels are required to equate protectionist activity with economic activity on a regular basis. The challenge for valuers is therefore to identify and adopt a methodology which will allow this substitution to occur.

Over a long period of time there has been a recognised market for items of jewellery, art work and more recently memorabilia associated with popular artists. A market has been established for such items through auction systems, and to some extent commercial hype. The fact that these items are perceived as having value largely relates to their scarcity and implies that there are market forces which recognise non-traditional items for sale.

Most cultural and natural "quality of life" values have in the past been less readily marketed and the protection of these things for the "public" good is often left to Government agencies. There is therefore a necessity to somehow attach a value to these items.

The examples used in this paper concentrate largely on an area known as the "High Country" of the South Island of New Zealand. This is a unique area of tussock grassland interspersed with mountain forest and other

vegetation. The landscape developed without the presence of grazing mammals and since the 1840's has been progressively grazed by the domesticated sheep, cattle and deer. It has also been subjected to grazing by various pest animals. The same environment holds a wealth of natural values and to a lesser extent cultural values relating not only to European settlement over the last 160 years but also Polynesian settlement over at least 1000 years. The description provided by Naughton (1991) summarises well the special nature of this environment when he says:

The South Island high country is regarded by many as one of our most distinctive landscapes. Stretching along the eastern flanks of the Southern Alps from Marlborough to Southland, these dominantly tussock covered mountains and basins create an open dramatic landscape, with the tawny yellows and browns of the tussocks contrasting sharply with the clear blue skies and often snow covered mountains beyond. Anyone driving from Christchurch south to Mount Cook or Queenstown cannot fail to be impressed by the wide open spacer in the MacKenzie or the subtle texturing of the Lindis Hills.

The high country also has many important ecological values with a number of plant and animal species confined to this environment.

In the conclusion to an earlier paper on a related topic Taylor

(1995) said: *The high country estate has many values, not all of which are recognised in the marketplace. The valuer has the task to identify what these values might be. In many instances they will reflect the move away from the high country estate being regarded solely as the domain of Merino sheep and Hereford cattle. Valuers working in this field must ensure that they are continually looking to new ways of assessing the intangible.*

CULTURAL HERITAGE:

As an introduction to the importance of cultural heritage reference is again made to Molesworth (1997) and with respect to other parties that he was quoting in his paper. *The preamble to the Convention concerning the Protection of World Cultural and Natural Heritage recites that the deterioration or disappearance of item of the cultural or natural heritage constitutes a harmful impoverishment of the heritage of all the nations of the world and that parts of 'the cultural and natural heritage are in such outstanding interest that there is a need for such parts to be preserved as part of the world heritage of mankind as a whole.*

This emphasis on the interest of human kind to the whole is carried forward into the Conventions definitions of cultural and natural heritage as found in Article 1 and Article 2.

Cultural heritage is defined as "monuments: architectural works, works of monumental sculpture

and painting, elements or structures of an archaeological nature, inscriptions, cave dwellings and combinations of features, which are of outstanding universal value from the point of view of history, art or science; ...

Many nations of the world have a long and recorded history associated with the presence of humankind. The recorded history of New Zealand by contrast is relatively short but this in no way denigrates from the wealth of cultural heritage that New Zealand enjoys. The original Polynesian settlers have a rich and varied history. Much of this history is held as secrets in the land itself. The heritage values that attach to this history are often difficult to measure and do not relate directly to the European monetary system. They are none the less a component of the mountain lands history that we deal with on a regular basis and in many cases recognition is required.

The European and Asian history of New Zealanders is an even more recent phenomena. Much of the history spans less than six generations but the impact on the land has been significant. There is a strong desire to protect such interests which is carried through to historic places legislation that recognises any artefact or structure over 100 years old as being of historic significance.

The factor of time as alluded to in the previous two paragraphs is of considerable interest and importance to valuers. The

perception of time has carried through into much economic and valuation theory. In the New Zealand context; does this place a greater value on the relics of Polynesian culture spanning periods in excess of 1000 years, or of European cultural relics with a history of little more than 100 years? In world wide context, with a much longer history how can relics be ranked in terms of value. In some cases the relics we are dealing with are of substance. These may range from the residences of early cave dwellers and the artwork history of such cultures, to the relatively recent "castles" of New Zealand. Lying between we have the wide range of cultural remnants of early ages which includes the temples of Asia, the structures of ancient Britain, to the grand cities of South America. Where the structures remain these may have some "use value" but where they are fragile relics the concept of value is more difficult to identify.

An example which is dealt with regularly in the high country scene of New Zealand relates to the early history of goldmining. The remnants in this case may range from the crude structures which formed the residences of the miners to many kilometres of hand dug water races to the deep shafts of reef mining. In some cases the values attached to these may be little more than the nuisance value of them imposing on a modern land use. In other cases they are recognised as an important part of culture. The cost of protecting such remnants versus the value of protection

may be a concept that the valuer has to grapple with.

NATURAL HERITAGE:

Continuing with the reference to Molesworth (1997): *Natural heritage is defined as natural features consisting of physical and biological formations or groups of such formations, which are of outstanding universal value from the aesthetic or scientific point of view.* It is in the realm of natural heritage that one encounters compensatory values more frequently. Often the natural features regarded as having outstanding value are also deemed to have some productive use. This is particularly the case with the conservation of flora. There is the familiar debate that has raged for many years over the clearing of native forests. These forests have a distinct commercial value and in some cases forested land has the potential to be cleared for agriculture. The forests also have high value to the overall ecology of areas and indeed the biosphere as a whole.

More recently there has been growing interest and concern about the world's tussock grassland. Again this paper draws on the New Zealand experience, with reference to Harding (1991): *Protection of the great tussock grasslands of the high country has been sadly neglected. The sweeping high country scenery so frequently painted and photographed, is gradually disappearing in many areas.* And from Mark (1982): *Unfortunately, natural ecosystems such as tussock grassland are*

irreplaceable. They can never be reconstituted once their sod has been turned. (The Americans recently have been investing much money and effort in an attempt to reconstitute a few small areas of tall grass prairie). Because of this often neglected aspect of non-replaceability and the continuing trend of development, efforts to retain adequate regional reserves of tussock grassland and other ecosystems must continue. Since tussock grasslands do not generate the high level of inspiration and public concern that our indigenous forests have achieved, the campaign for reservation must be waged by a relatively small group, mostly scientists.

Since 1982 there has been growing recognition of the importance of tussock grasslands and for the purposes of valuation we draw our attention to two examples. The first is an area where a Government agency chose to use its legislative power to protect an area of tussock grassland with high conservation value. The legislative designation for this area proceeded through a number of required hearings, but eventually led to a negotiated partial protection. The cost to both protection agency and current landowners was extremely high. The second example relates to an area which has been recognised for its high conservation values over a period of some 15 years. The protection agencies in this case pursued a process of negotiation using some tradable

rights they already had under land tenure. This led to a total protection of the values identified, and was achieved at a modest cost.

A second aspect of natural heritage relates to the indigenous fauna of a country or locality. Most countries have identified lists of species that are either at risk or are highly endangered. Most nations can also identify a loss of faunistic species over the past century. The requirement of habitat protection for birds, insects and animals is less clearly established than that of identified vegetative species. Many animal species require extensive habitats to maintain themselves. While the protection of habitat could be measured against the alternative use by domestic stock or human endeavour the actual value associated with the loss of the species to the world wide genetic pool is not measurable.

As an example a wading bird that is endemic to a particular locality. This wading bird has very specific habitat requirements and generally nests in open riverbed areas. In this case most of the riverbed lands are already in Crown ownership but the introduction of various plant species to the habitat has reduced the breeding potential of this bird. In order to protect the species considerable sums of money have been spent redeveloping a "natural" riverbed system. Another example relates to a large lizard found in a very limited region. The lizard has generally been identified on large rock

outcrops and some of the rock outcrops have been protected from damage by humans. Numbers of this species have continued to decline as it became apparent that the total range of these lizards was considerably greater than in those areas on which they were generally identified. Grazing by domestic stock has reduced the habitat, and removal of these stock has an measurable value. Again the protection of the species is immeasurable.

Landform conservation is important to many Pacific Rim countries. Landform often forms the background and the attraction for tourist visitors. Some human activities have a tendency to alter the natural landforms and therefore damage many of the exciting areas which attract tourists.

To use a tussock grassland example, there is a well known tourist route that passes through a mountainous area. The natural vegetation has long been a feature of this area and has been widely photographed by visitors. Continued grazing pressure by domestic and feral animals has the potential to reduce the natural cover of this area. As a valuation exercise there is a direct cost to a farmer of reducing the stock using this sensitive area. This can provide one measure of value, however, if the area is irreparably damaged then it may have additional community costs in terms of visitor appreciation. This is more difficult to measure.

A final area of natural heritage

values that must be considered relates to soil and water conservation. A nation's primary production relates to directly to its soil resource. The loss of the soil resource and therefore the loss of primary production, the essentials of life; food and water is critical to a nation's survival. For many years the *Law of the Commons* has been cited in this regard and it is difficult for a single generation to recognise the cost of management practices which significantly reduce this base. This aspect of heritage brings a direct relevance of time into the valuation equation.

Often tied to soil is water management. Many nations are experiencing acute shortage of fresh water for drinking and industrial purposes. This can be both through catchment loss and also through pollution. A particular aspect of catchment protection recently arose, again in the tussock grassland heritage. In this particular case there was some value to the nation from flora conservation but this had a considerable added value for the protection of a water supply to a major city. The combined values far outweighed any value for continued commercial use.

In identifying value attached to heritage values, the valuer has to recognise a wide range of individual and societal perceptions. These perceptions can arise from cultural, spiritual or educational background. In many cases decision making on protection of both cultural and natural heritage values involves

public consultation. Such consultation often cause wide ranging views of particular values. These generally range from those who regularly involve themselves in the landscape and have an appreciation of the naturalness of what they are looking at. Others may perceive the environment purely from its scientific uniqueness. A third group, and often more difficult to identify and quantify has an appreciation of natural values, and often heritage values purely from knowing that such things exist. They may never visit these areas nor have any particular scientific bent. They have at some point in their life perceived that such areas have importance and interest and are content to know that they exist.

HERITAGE MEETS COMMERCIALISM:

With the growing "green" aspirations of many of the world's citizens conservation can become a commercial reality. Aspects of heritage do attract visitors and the management of visitors can become a commercial concern. This can range from the simple Government provided visitor centre, often with a donation box attached, to highly commercial operations.

To draw on an example used by Dunckley (1993) where he investigated the market related values attached to a wildlife reserve. In this particular case a commercial organisation had established a visitor's centre and an opportunity for viewing a giant albatross colony at Taiaroa Head

in Otago, New Zealand. In this paper the value of the wildlife sanctuary was really related to the concession fees paid by a third party to the Crown.

Dunckley identifies under the heading "Value of the Sanctuary": *The concession paid to the Department of Conservation by the Otago Peninsula Trust represents one element of value. The headland with its wildlife and history has an added value to:*

- Conservation - on a local national and international level.
- Tourism local and national.
- People of New Zealand and pre and post European settlement.

The Taiaroa Head site is of significant "spot" location value which is in addition to but pre-dates the current commercial operation. Can the values be assessed? If they can is the sum of the fair identifiable values added to determine the overall value?

A cashflow approach cannot represent the meaning of the headland to the Maori people. Money simply could not buy, nor represent the value. The scale of value is measured differently. It is a humble and subtle value which can never be destroyed or replaced. This is identified as an important part to Taiaroa Head.

Dunckley then proceeds to identify an assessment of value based on the tourist concession.

On the surface this may appear to be at odds with the above statement. It is however tacit recognition that in spite of social philosophy the valuer is charged with developing tools to value the invaluable.

Protection of heritage values, commercial uses substituted by those values, and concessions related to those values do provide an indication of worth but not necessarily value.

LEGISLATION:

Before examining the valuation context in more detail there is one more aspect to be considered which tends to create a clouded picture for valuation input.

A common approach to securing heritage and cultural values for the benefit of the population is for Governments to adopt legislation which ensures this protection. This often has the effect of distorting market values. Many countries have enacted legislation to ensure appropriate management of resources for the benefit of future generations.

In New Zealand this legislation includes the Resource Management Act of 1991. The purpose of this Act is to promote the sustainable management of natural and physical resources. By interpretation it therefore has some application to the protection of areas with high heritage values. Similarly public access to important waterways has been created through the Conservation Act 1987. In the case of leasehold land this latter legislation has

particular impact in that such access is created automatically on renewal of the lease. As the access is not specifically excluded from the lease it provides a difficult valuation equation.

The use of legislation versus market forces raises the issue of whether natural and cultural heritage values are best managed by the ownership of the Crown or through some arrangement with other land occupiers. In recent years much has been written on this topic. In particular Ackroyd and Hide (1990) wrote specifically about the leasehold pastoral lands of New Zealand.

Page 3: The contest over the resource involves some fundamental questions regarding the rights already conferred over pastoral land, the rights retained by the Crown, and the nature of the public's interest in the resource. However the contest for the resource is nothing new. The history of pastoral land management in New Zealand has been a history of continual changes to rights to the resource as Government sought to reconcile public ownership with the public interest.

Page 19: The idea that land identified as having conservation value should be automatically protected is a nonsense. Protected natural area surveys can compare different areas to assess their relative merit in terms of nature conservation, but they cannot assign a value to nature conservation itself. They cannot tell whether the areas

recommended for protection should be protected or not. What ought to be done with a resource cannot be logically be inferred from what the resource is.

Page 23: Reports prepared to assess high country values and recommend land use can only reflect their expert authors idiosyncratic preferences, in the final carve up itself will be decided by contests at a political level.

And: At present nature conservation and recreation are considered in non-commercial uses, not because of the inherent nature of these uses, but because Government has taken it upon itself to provide for them. In contention is not how a Government should best provide for nature conservation and recreation, but whether responsibility should lie with those with a direct interest in nature conservation and recreation.

This dialogue of ownership versus management creates a new concept in the valuation arena. This also increases the range of tools available in managing land use. The New Zealand Land Act of 1948 established leasehold tenures over much of the high country land. This established certain property rights for the pastoral farmer but retained ownership of the resource with the Crown. A programme is currently underway in New Zealand to review these leases. The basic premise on which this review is being carried out is that commercial and conservation interests should be separated.

This implies that there are only two end results; being freehold land held by a commercial user, and conservation land retained by the Crown. In reality the issue of ownership versus management requires a middle ground. This often includes the use of leases which specify particular land rights to the farmer while protecting conservation interests to providing land ownership to the farmer with covenant protection of conservation interests. To ensure equity between the parties each of these variations require valuing.

**INTERNATIONAL
INFLUENCE:**

There are very real elements of an

overall world economy developing. This relates as much to heritage values as it does to economic values.

There are a significant group of people who have grown up in a very un-natural situation, the concrete jungles and pavements of our major cities. A significant number of these people look to other less developed nations for their recreation and spiritual restoration. A weekend at some of the major golf courses or fishing localities of many Pacific nations will show a very international favour. Where the land laws of particular countries allow foreign ownership and residency of their lands there can be noted an

increasing international ownership structure. In the past this has tended to predominantly exist in relation to commercial operations but there is a growing trend for the international entrepreneur to wish to occupy a retreat in some foreign land. The values attached to this retreat are often totally different to those of the residents or citizens of those countries. This creates a new component to valuing special places and special values.

SS

April

The World Congress Trust (UK) has nominated MELBOURNE as the venue for the forthcoming World Valuation Congress Vill. Hosted by RMIT with the theme being Present Values and Future prospects

The Congress is being supported by both the National and Victorian Division of the API. Eminent speakers from the UK, Africa, Asia and New Zealand as well as from Australia have been secured and submissions to present papers have been received from the UK, US, Canada, Asia, Africa, Hong Kong and Australia and more are welcome.

Further details may be obtained from John Leigh, Property Group, RMIT,
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APPROACHES TO VALUATION

This discussion related to the resource which is being considered and identified a number of issues relating to valuation. Attention now turns to methodology for accommodating these values. While there is some sympathy with the previously quoted paper by Molesworth, many economies have moved to considering heritage values as assets which can be traded and can enter balance sheets.

RESOURCE ECONOMICS:

This field of economics has been taught to resource managers since the late 1970's. Since this time a number of authors have focused their attention on this issue. Most recently Molesworth (1997) in his conclusion stated: *Modern economic theory has a tendency to under value the non-tangible values that are inherent in heritage places and objects. At the very best, modern economics is clumsy when faced with the task of balancing the values of one against the values of another. Somewhat artificial methods of arriving at hypothetical economic values have been awkwardly promoted. As a consequence, at differing levels of threat, Governments around the world are demanding their land managers or their heritage custodians more and more onerous obligations to justify the protective and supposedly more restrictive, measures intended to safeguard heritage.*

In my opinion the economic barbarians understanding of

cultural values and natural values is often so sadly deficient that there is an ongoing obligation on the shoulders of those charged with responsibility to protect heritage to be ever vigilant to resist the tendency for Governments to enact legislation or put in place administrative arrangements that would allow the comparison of "chalk with cheese". In conclusion, whatever the particular legislative model adopted to protect heritage, the most essential requirement is that the procedures adopted must be empower decision makers to give due weighting to intangible values, the often indescribable but none the less real values, inherent in the places and things we wish to keep for future generations.

Bond (1993) summarised a paper on the topic with the following comment:

The valuation profession needs to enlarge its definition of "market value" taken from a merely economic viewpoint, to encompass the more intangible aspects of property.

Present definitions are based on assumptions that ignore social concerns. For example, the "highest and best use" is that use which earns the most money, yet it ignores the effect of use on the environment.

Also "market value" as determined by one or more of the three conventional valuation

methods, is based on the assumption that the property is marketable.

However, specialised property for which little demand exists, is not marketable. Such property is held for owner occupation or for servicing the community and not for pecuniary benefit. It has a high utility value but may have little or no exchange value.

Bond earlier in the same paper had quoted Kerr (1986) with his discussion of four techniques of valuation:

1. Contingent valuation which involves surveying people to determine their willingness to pay for a possible change in markets and supply or quality of non-market goods. The valuation is "contingent" on specific hypothetical change identified.

2. Travels costs method which estimates the aggregate demand curve of a site and rests on the assumption that the use of the site is dependent solely upon the travel costs to it. Should the price of travel to reach a site increase it is assumed the use of the site will decrease.

3. Indifference curve mapping which relies on interviews with subjects that are often long and difficult to conduct. This is primarily due to the explanation of probability that is required which many subjects find difficult to understand.

4. Hedonic price method which assumes that the price of a property is determined by the characteristics, such as: number

of bedrooms, age, construction et cetera. The method uses statistical means to estimate the marginal value of some environmental characteristics that are part of the package. These methods are commonly used in resource economics and by resource managers. They are often attempts of such people to put in a box something that doesn't fit.

Having stated the above it is necessary to review some of the components which may make up values for these intangibles or heritage or non-productive items. Placed in the context of the pastoral lands review of the South Island high country of New Zealand these concepts take on some relevance.

Taylor (1995) identified a wide range of "values" which can contribute to this picture, as shown in Figure 1:

HIGHEST AND BEST USE:

Highest and Best use in this context is used more as a perceived public benefit than the standard economic benefit.

The example in figure 1 is a departure from both the historical "market" for mountain lands and traditional valuation approaches. A decision was made progressively from the days of early New Zealand settlement through to the 1950's that the best use of high country tussock grasslands was pastoral farming and this was enshrined in the current tenure system. Some specific areas had been excluded for national parks or reserve benefit but these did not generally conflict

with commercial use of the land. It is assumed that pastoralism was the highest and best use.

The development of the nation in the late twentieth century has placed a different perspective of value on these lands. It has been estimated that some 40% of the land currently utilised for pastoral farming has an alternative use of nature conservation or public recreation. The remainder may have a wide range of commercial uses which bear little resemblance to that provided for in current leases. As previously noted there is a programme underway at present to identify and separate these values. This has created a new "market" for such land. Existing property rights have forced land managers to consider an upset price greater than that which could be attached to the land for its pastoral farming use.

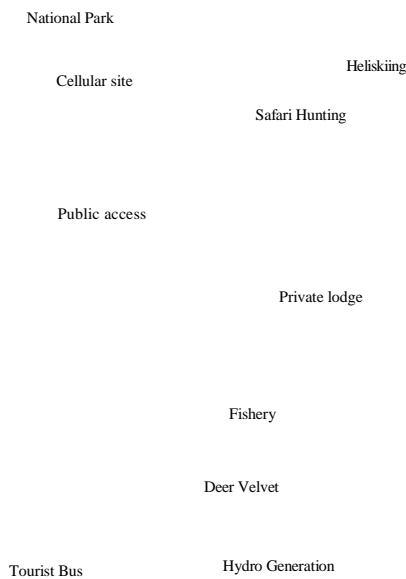
The use of the term "high inherent values" in proposed legislation has alerted current land occupiers to an expectation that the protection of these values may have value. The difficulty with using this method is that it undermines the principle of bona fide sale in that there is generally only a single buyer in the market and that the seller is reluctant. It must also be noted that the exchange of benefit and property rights vary from situation to situation and this further distorts any attempt at market analysis.

DISCOUNTED FUTURE BENEFITS:

The use of discounted future benefits is a valuation technique well known to those working in the commercial and industrial areas. It has not commonly been applied in rural valuation. In this field values per hectare of arable

Figure 1

Components of High Country Value



land or per stock unit grazed are commonly used.

Dunckley (1995) concluded that: *Valuing conservation assets brings perspectives of both the past and the future into the present.* In this paper he identified that commercial discount rates lead to a diminishing return over time. Conversely heritage values or conservation values attract a very low or negative discount rate and tend to appreciate in value with time. These relationships identify a particular point at which conservation will show a greater benefit than production. While the discounted future benefits equation has merits in assessing one value against another, in this case conservation versus commercial use the methodology has some limitation where there are many components making up the overall interest. The important concept introduced here is, however, that of time, which is the feature that makes heritage values stand apart from those of a commercial nature.

TRADITIONAL ECONOMICS:

Webber (1992) approached the valuation of un-priced resources from the viewpoint of an economist. He noted three types of value which should be considered

The first value is use value. This is an economic value that can be measured through preferences. Anglers, hunters, trappers, bird watches all use the natural environment and all derive a benefit for a value related to this use. The second type of value is

option. These are values expressed through an option to use the natural environment. This is a potential benefit rather than an actual use value - an expression of preference for the preservation of an environment against some probability that the individual will make use of it at a later date.

Option value arises from uncertainty. Given that people do not like risk and uncertainty, individuals are willing to pay more than their use value just to ensure that they can make use of the natural environment at a later time.

The third type of value is existence value. This is the value that resides "in" something and is captured by preferences for non-use values. Existence value is concern for the rights or welfare of non-human beings, the values of which are unrelated to human use. An example of this is the value people place on saving the remaining blue whales; few people will value these whales because they use them or want to preserve an option to use them.

Total economic value can be expressed as the sum of use value plus option value plus existent value.

This approach relates closely to reality. As part of the process of rationalising land use and tenure the wider public are asked to comment. The submissions received give a lead on public perception and if not a definitive value of the heritage, at least a ranking of importance.

VALUING HERITAGE:

Valuers and economists have attached value to non-productive assets and in particular heritage values for a number of years. As the twentieth century draws to a close there is an increasing desire for Governments and other agencies to measure heritage values against the more easily defined commercial values. This trend has been noted by a number of authors and various attempts have been made to quantify the values that can be attached to such pressures. Most of these writings have tended to confine their analysis to the direct compensatory value which exists between commercial and non-commercial assets. It must however be recognised that this area of valuation is complex and that often multiple values will contribute.

Figure 2 is a graph of a standard approach. At the intersection of the graphed lines substitution between uses will occur and the concept of "value" is satisfied. Other uses do not enter the equation as they do not generate enough value to register on the scale.

The grids adopted in this graph are purely relative. The term "relative time" is used to reflect both a discounting period and the tendency for items of cultural heritage to gain value with age and for those of natural heritage to become increasingly rare with time.

From a base of 100 the current established use dominates. Property rights determine the availability of alternative uses. The traditional commercial use

shows a standard reduction in value of time using standard discounting techniques.

Species protection is the catch cry of the nineties and reflects the three perceptions of value identified in the earlier quote from Webber(1992) - use, option, and existence value. With a perceived increase in value as rarity is confirmed over time, the value of "protection" escalates. The extreme of this is that the focus of protection becomes "priceless" and the role of the valuer will be limited to cross referencing with what happened in a similar situation on a previous occasion. The same will apply to rare items of culture.

Landscape is often at less "risk" and tends to reflect a more constant value. Recreation may show an initial lift in perceived value and then remain relatively constant. The graph has been limited to four essentially rural examples to avoid clutter, but can

be enlarged or shrunk to reflect the individual situation of the valuation. Commercial real estate housed in historic buildings could be subjected to a similar approach. Identifying the range of options that may apply in a particular situation requires valuers to remove the constraints of traditional training and look to other disciplines and sound local knowledge balance with market research. Secondly the skill of the valuer in identifying the correct equation for each potential use is paramount.

There are many well established lobby groups with diverse interests in heritage values. Each group tends to have a particular focus. Where single heritage interest does not carry sufficient weight to bring about a substitution of use these lobby groups often join together to create a combined case. Figure 3 using the same data highlights this effect with the combined conservation value equalling the

commercial value at a much earlier point.

Increasingly even this approach may be inadequate as not only heritage value but also commercial resources become more scarce. Single use substitution may be an easier concept to grasp, but multiple use of resources is often an alternative which must bear consideration. This introduces a new realm to the valuation equation. Figure 4 uses the same data that was applied in Figures 2 and 3, but applies this to the multiple use concept. The earlier effects of time and rarity are not lost, but the added realm of multiple value applies.

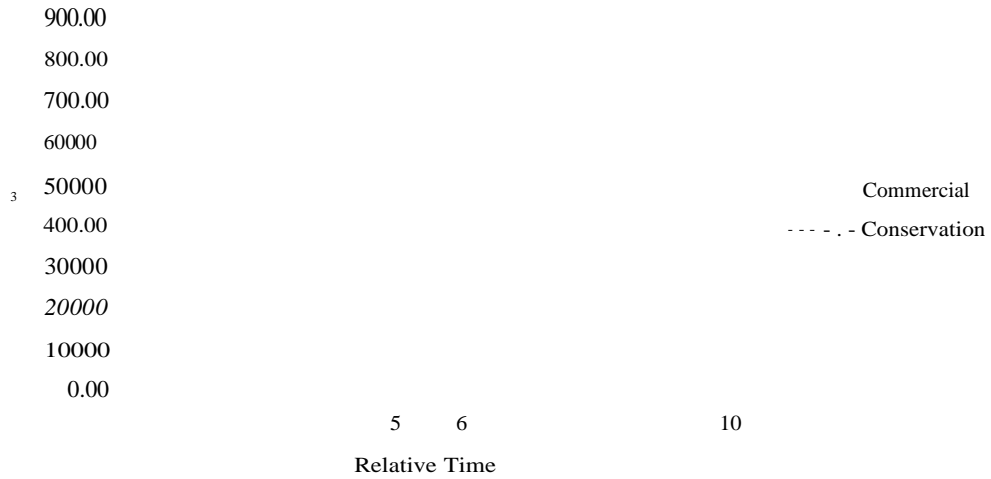
CONCLUSIONS:

It is the contention of this paper that the valuing of non-commercial assets is not easily defined in the normal rules that professional bodies apply to the valuation of assets. In both the

rural and urban valuation fields, unexplained variations. These what has for generations appeared can relate to a cultural or ascetic a simple matter of valuing land, vision held by the purchaser or bricks and mortar may miss the the vendor towards some aspect point. It must be recognised that of heritage. even in the traditional sales The professional valuer is analysis there are often

charged with:
 Firstly identifying all the components which may apply to the individual site.
 Secondly identifying the relationship of each component to all others.

Figure 3: Combination Approach



Thirdly applying the correct time/value equation to each component. Fourthly recognising when to stop valuing the invaluable.

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About the author

Ken Taylor is the Branch Manager of Knight Frank (NZ) Limited, Alexandra. He holds degrees in valuation and resource management from Lincoln College, University of Canterbury, is an Associate of the New Zealand Institute of Valuers and has practised as a valuer for over 20 years. He is also a Fellow of the New Zealand Society of Farm Management.

Employed by the Department of Lands and Survey for nearly 12 years before Ken joined the property company now known as Knight Frank in 1987. Throughout his career he has had a close association with the mountain lands. Ken is currently involved in a contract with the New Zealand Government identifying and negotiating a separation of heritage and commercial values.

CUSTOMARY RIGHTS TO TROUT - *THE McRITCHIE LITIGATION*

Gerald Lanning

BACKGROUND

In early 1995, Mr McRitchie went fishing in the Mangawhero River. Nobody expected the controversy it would raise. Nor did anyone expect that it would result in litigation that would reach the Court of Appeal.

While fishing Mr McRitchie was approached by a Fish and Game Ranger. Mr McRitchie admitted he was trying to catch trout and that he did not have a licence. He also told the Ranger that because he was from the local hapu (who hold mana whenua over the area in which he was fishing) he thought that he did not need a licence. However, the Ranger issued an offence notice and consequently Mr McRitchie was charged with two breaches of the Conservation Act 1987, namely:

using prohibited fishing tackle; and
fishing for trout while not holding the required licence.

For technical reasons (not discussed in this paper), the first charge was withdrawn. The charge of fishing for trout without a licence is a charge of a breach of section 26Z of the

Conservation Act which states:-

"Subject to this Act, every person commits an offence and is liable to a fine not exceeding \$5, 000, who- takes sports fish from any fresh water at any time, unless that person is the holder of a licence issued under this Act, authorising him or her to take such fish from such waters at such time," (emphasis added)

Mr McRitchie's defence was based on two sections of the Conservation Act, namely sections 4 and 26ZH. Section 4 incorporates principles of the Treaty of Waitangi ("the Treaty") into the Act. Furthermore, section 26ZH purports to protect "*Maori fishing rights*". In short, Mr McRitchie claimed that he did not require a licence because he, as a member of the local hapu, had an inherent right to fish in the river and catch trout and that right was preserved by the Conservation Act.

This article firstly traces the litigation and, in particular, the reasoning of all of the judges involved. Secondly, there is some analysis of the important legal issues which arose.

JUDGE BEECROFT'S
DECISION

The matter first came before Judge Beecroft in the District Court at Whanganui. According to Judge Beecroft the "ultimate issue" for determination was

"...whether a Maori charged under section 26ZI..... of the Conservation Act....while fishing for fresh water fish (trout) without the required licence, can rely on:

"Maori fishing rights", (Section 26ZH of the Act); and/or

the "principles of the Treaty of Waitangi", (Section 4 of the Act) as a defence to the charge, given that trout are not an indigenous species and were introduced after the signing of the Treaty.

There is a customary right to fish for indigenous fish.

Section 26ZH of the Conservation Act states that "nothing in this part of this Act shall affect any Maori fishing rights." The offence with which Mr McRitchie was charged was within the relevant part of the Act. Section 26ZH is the exact wording previously contained in section 88 (2) of the Fisheries Act 1983. Based on a well established line of case law that discussed that section, Judge Beecroft concluded that if Mr McRitchie had been fishing for indigenous fish, then the defence would have succeeded because Mr McRitchie was:

- A Maori from "hapu and iwi with authority" over the relevant area; and

Fishing in accordance with the local kawa or protocol; and

Fishing *"for personal use consistent with principles of conservation and preservation."*

So the question became whether the defence could extend to a situation where the fish is not indigenous but introduced after the Treaty.

The right to fish for indigenous fish extends to introduced fish. Section 4 of the Conservation Act directs that:

"This Act shall be so interpreted and administered so as to give effect to the principles of the Treaty of Waitangi."

Both the Court of Appeal and Privy Council have held that "the principles of the Treaty" include "the express terms of the Treaty." The Treaty expressly preserves (under Article II) for Maori their "full, exclusive and undisturbed possession" of "their fisheries."

After considering the Waitangi Tribunal's *Muriwhenua Fishing Report (1988)*, his Honour concluded that the term "their fisheries" refers to "more than just species of fish caught as at 1840." Instead that term encompassed:

"...the activity and business of fishing, the place where fish were caught and the right to take fish."

Thus, the right to the "fishery" is much broader than the mere right

to fish for a certain species of fish within the fishery. At first sight, therefore, the Maori rights under the Treaty to "their fisheries" includes a right to fish for trout and the timing of when trout was introduced seems irrelevant.

The Fish and Game Council argued that any Treaty right should be restricted to the species existing, and the methods used, in 1840. Judge Beecroft rejected this argument and found support in a number of Court of Appeal decisions regarding the interpretation of Maori customary and Treaty rights. Accordingly he concluded:

"The clear principles enunciated in the series of leading Court of Appeal cases, do not seem inconsistent with trout, an introduced species, being included within the right. My preference is to include trout within that right. However one important issue remains for consideration. That issue, is whether the fresh water fisheries legislation explicitly excludes trout from '...any Maori fishing rights'." (emphasis added).

Earlier in his decision Judge Beecroft discussed whether this right was sourced in the common law doctrine of "aboriginal" (or "customary") title or the Treaty. His Honour expressed a preference that section 26ZH expressly protected aboriginal rights. However, in the end the source of the right was not relevant - whether it was a customary right or a Treaty right - there was an inherent right to fish for trout.

Such rights can be extinguished by (among other things) legislation that shows a "clear and plain intention" to do so. Therefore, it was necessary to examine the legislation that had purported to control trout. Interestingly, Judge Beecroft noted that *"this aspect of the case has caused me the greatest concern."* It was this "aspect of the case" that would split the opinion of the Court of Appeal. However, after reviewing the legislation, his Honour concluded that the legislation did not expressly limit or restrict any right to fish for trout. Accordingly, the right to fish for trout had not been extinguished by the legislation and so the charge against Mr McRitchie was discharged.

On any reasonable analysis this was a bold decision. In fact Justice Thomas (in the Court of Appeal) described Judge Beecroft's decision as *"courageous"*. Judge Beecroft accepted that his decision was *"at what might be called 'the liberal' end of the spectrum."* Furthermore, he acknowledged that *"the issue is not clear-cut"* and that *"value judgements are involved."* These comments were later proved true when the issues came before the Court of Appeal. However, before reaching the Court of Appeal there was an appeal by the Fish and Game Council to the High Court.

THE HIGH COURT DECISION

No doubt because of the importance of the issues, two

judges sat to hear the Fish and Game Council's appeal. The High Court took quite a narrow approach to the issues and focused almost solely on the legislation that had purported to control trout.

The High Court impliedly agreed that, it was at least possible that Maori fishing rights extended to *"the available fish, the places where fish were caught and the methods and practice offishing"*. Accordingly the High Court could, on the face of it, see nothing wrong with Maori fishing rights extending to trout. However, after an extensive review of the relevant legislation it was the High Court's firm view that:

"successive legislation had the effect that there was never a time when trout or salmon were available without control to those who otherwise were free to or had rights to fish in fresh water".

Accordingly, there was never a time when the taking of trout could be regarded as an existing and preserved Maori right. Unhappy with this decision, Mr McRitchie appealed to the Court of Appeal.

THE COURT OF APPEAL'S DECISION

Five Court of Appeal Judges sat to determine Mr McRitchie's appeal. In short, four of the Judges ("the majority") agreed with the High Court decision. However, Justice Thomas

("Thomas J") dissented.

The focus of the majority's decision was (as in the High Court) the history of legislation controlling trout. They concluded that a necessary implication of the legislation was that there were never any Maori fishing rights in respect of trout.

However, significantly, as in the High Court the majority of the Court of Appeal impliedly accepted the proposition that Maori fishing rights could extend to fish introduced to New Zealand after the Treaty.

JUSTICE THOMAS' DISSENT

Justice Thomas firmly disagreed with the majority's decision. Two themes emerge from this dissent, namely that:

- The fundamental constitutional status of the Treaty and in particular its protection of Tino Rangatiratanga (jurisdiction) and Maori rights in respect of their Taonga (resources); and
- The need for these fundamental rights to be protected.

The "real issue" what Maori are seeking defining the right.

Thomas J began by discussing what he saw as the "real issue."

"What Maori assert is their mana whenua and Tino Rangatiratanga over the river. By the assertion of mana whenua, Maori seek recognition of the power and influence associated with the possession of their taonga, the fishery, and if its capacity, carefully sustained, to produce food for whanau, hapu and iwi."

By Tino Rangatiratango Maori ask for acceptance of their mana or authority or control over the river or fishery At the very least it is a plea for their right to participate in the control of the river in accordance with the principles of the Treaty as defined by this Court...

The authority or right to control or participate in control does not disappear simply because trout have been introduced into the fishery. "

There was insufficient evidence to determine the actual nature and scope of Mr McRitchie's hapu's customary and Treaty fishing rights. However, for the purposes of argument it was assumed by Justice Thomas that the right to fish for trout without a licence did exist.

Thomas J reminded the Court of the dramatic change in attitudes towards Maori rights and referred to the *"restrictive approach of earlier Courts which the judiciary now bear with ignominy and discomfiture. "*

Extinguishing the rights

Thomas J was determined to ensure that Maori customary and Treaty rights were protected. By adopting the court's attitude to protecting the citizens' traditional right to privacy in the home, it was his Honour's firm view that:

"..... in order to extinguish or curtail a Maori fishing right or right protected by the Treaty, the legislature not only must direct its attention to the question of

extinguishing or curtailing that right but also must deliberately determine that it should be extinguished or curtailed. The intention must be clearly manifested by unmistakable and unambiguous language. "

Here, Justice Thomas set a far more restrictive test than that applied by the majority. While the majority were happy to extinguish a Maori fishing right by "necessary implication", Justice Thomas applied a test that required Parliament to do three things. According to Justice Thomas, before a Maori fishing right can be extinguished or curtailed, parliament must:

Direct its attention to the question of extinguishing or curtailing the right; and

Deliberately determine that the right should be extinguished or curtailed; and
Manifest its attention by unmistakable and unambiguous language.

Justice Thomas went on to explain the policy reasons for applying such a strict test. In essence, his Honour was concerned that judicial implication would deny Maori and other interested citizens the opportunity to participate in the democratic and parliamentary process. Just like all the other Judges, Justice Thomas carefully reviewed the relevant legislation. Before doing so, his Honour criticised the reliance the High Court and majority of the Court of Appeal had placed on historic legislation and subordinate legislation.

The purposes of analysing historic legislation is to deduce parliamentary intent. With respect to Maori property rights it was his Honour's opinion that, *"it is fair to say that people, including legislators, are much more enlightened today than when the historical legislation was enacted. "* Accordingly, Justice Thomas asked the following question:

"Why, then, in order to arrive at a statutory implication, should Parliament be fixed with a pre-enlightened approach to fishing and Treaty rights especially when the current legislation expressly reserves Maori fishing rights and directs that the Act is to be "interpreted " so as to give effect to the principles of the Treaty. "

The Fish and Game Council placed some reliance on subordinate legislation (i.e. regulations) as support for its contention that legislation had overridden any Maori fishing right in respect of trout. Most statutes delegate power to the Governor General to make regulations on certain matters. Those matters usually related to matters of detail that may change from time to time. In general, regulations are made by the Governor General on the advice of the executive (i.e. the Minister). Therefore, parliament is not involved and, in Thomas J's view:

"The tail should not be permitted to wag the dog. Any direction that customary Maori fishing rights and rights under the Treaty are extinguished or curtailed should come directly from

parliament and not the executive branch exercising delegated authority only. "

Justice Thomas reviewed exactly the same legislation that have been reviewed by the High Court and the majority of the Court of Appeal. In contrast to those judges his Honour concluded that with the relevant statues either:

were consistent with the recognition of a right for Maori to control or participate in the control of ifshing for trout; or recognise that Maori have a right to fish for trout.

Therefore Justice Thomas could not agree that it was a "necessary implication" of the legislation that Maori fishing rights or rights protected by the Treaty had been extinguished or curtailed. It is useful to quote his Honour's conclusions at length:

"To my mind, sections 4 and 26ZH of the Act must be taken to reflect Parliament's current attitude and intention in respect of Maori fishing rights and the rights or interests secured by the Treaty. Section 4 recognises the fundamental constitutional status of the Treaty, and it and section 26ZH are not to be demeaned. Parliament should not be thought to have enacted these provisions as mere window-dressing. If therefore, it is found the guarantee of "their fisheries" to Maori under the Treaty includes the right to fish for food, irrespective of the species inhabiting the particular

fishery, Section 4 requires effect to be given to that guarantee. It requires the Act to be 'interpreted' as well as administered to give effect to the principles of the Treaty. Similarly, if it is found that the appellants' hapu have customary rights in the Mangawhero river which are not specific to any particular species, then section 26ZH clearly intends that the right will not be affected by any provision in Part VB of the Act relating to fresh water fisheries and the control of "sports fish ". The paramount direction from Parliament must be the specific provisions contained in sections 4 and 26ZH, and I would decline to read into the Act an implication that these sections do not apply to the provisions which, apart from section 26ZG defining the application of Part VB and 26ZH itself, largely relate to the regulation and control of "sports fish ".

SOMETHOUGHTS

To summarise, the High Court and the majority of Court of Appeal held that:

- Maori do have customary or Treaty rights to "their fisheries " which includes fish introduced after the Treaty; however,
- in the case of trout, the legislative history necessarily implied that trout were excluded from those rights.

In contrast Justice Thomas and Judge Beecroft held that:

- Maori do have a right to fish for trout; and
- the legislative history does

not imply a clear Parliamentary intent that the rights to trout should be curtailed or extinguished.

There are two important broad issues which emerge from the McRitchie litigation:

- What is the scope and nature of Maori fishing rights?; and
- How easily can those rights be extinguished or curtailed?

The scope and nature of Maori fishing rights
The right attaches to the "fishery "

The Fish and Game Council argued in all three Courts that Maori fishing rights should be restricted to rights existing at 1840 (when the Treaty was signed). The basis of this argument was that:

- Only indigenous species are part of the right and not species introduced after the Treaty; and
- Only naturally evolving "methods" of fishing based on traditional fishing practices can be used to exercise the right.

It is clear that all three Courts were at least open to the proposition that Maori fishing rights extended to fish introduced after the Treaty. Essentially that was because the right attached to "the fishery" rather than specific fish within the ifshery. If so, it would seem that the right to the fishery would also encompass a right to choose the

methods and places used for fishing.

The right to development

That conclusion is consistent with the notion of a "right to development". The Waitangi Tribunal has consistently upheld the principle that the Treaty preserves a right of development. Examples include the right to develop sea fisheries, geothermal resources and rivers. In the latest Waitangi Tribunal report to discuss the right to development, the *Te Ika Whenua Rivers Report 1998*, the Tribunal stated that it:

'firmly supports the principle that the rights to property and taonga preserved and guaranteed under the Treaty included a right to development

The Tribunal went on to conclude that the claimants had a right to develop their river resources (Rangitaiki, Whaeo and Whirinaki Rivers). Furthermore the Crown had interfered with that right by, for example, building hydro-electric power stations along the Rangitaiki River and imposing restrictions on fishing. The Court of Appeal, too, has impliedly accepted this principle by acknowledging a need to adapt and apply the Treaty in light of present day circumstances. For example in 1990 the Court of Appeal held that coal was a taonga and Tainui Maori were:

"entitled to the equivalent of a substantial proportion but still considerably less than half of this particular [coal] resource could be suggested as falling within the

spirit of the Treaty of Waitangi. "

According to Thomas J Treaty rights are fundamental

With respect to the nature of Treaty rights Justice Thomas was forceful in his assertion that the rights were "fundamental". Underlying his Honour's judgement was a concern that the Courts should not take a backward step from the recognition of Maori rights demonstrated by the Courts in the recent past. Justice Thomas referred the Treaty as *"this nation's founding constitutional document"*. It followed that the rights protected in such a document could be classed as "fundamental". As a consequence Justice Thomas had no difficulty imposing a very strict test as to whether legislation extinguished or curtailed such fundamental rights.

How easily can Maori Treaty rights be extinguished or curtailed?

The test applied by the High Court and majority of the Court of appeal is whether the legislation necessarily implies a clear parliamentary intention that customary rights should be extinguished or curtailed. That is broadly consistent with a number of cases throughout the Commonwealth. However, those cases were all decided with respect to customary rights not rights protected by the Treaty. Furthermore, a number of those cases state that "clear and unambiguous words" must exist before Parliament will be imputed with an intention to extinguish customary rights. It is important

to note that none of the legislation on controlling trout expressly extinguished or curtailed Maori fishing rights.

Justice Thomas could see no reason by rights protected by the Treaty should have any less protection than the right to privacy in our homes. That latter right can only be interfered with by clear and express words to that effect. In this context the words of Lord Scarman from the House of Lord's decision are relevant:

....it is not the task of judges, exercising their ingenuity in the field of implication, to go further in the invasion of fundamental private rights and liberties than Parliament has expressly authorised. The importance of express provisions is that it affords the citizen the opportunity, if he chooses to use it, to read and understand the extent to which his right and liberties have been curtailed".

As with Justice Thomas, underlying Lord Scarman's reasoning, was a conclusion that the rights in question were "fundamental". Accordingly, if there is any doubt as to the meaning of the legislation, the Court should not get involved. Rather the matter should be left to Parliament.

It is submitted that, whatever one's view of the outcome is, this is the sensible approach because the fundamental issue in this case was the status of rights protected by the Treaty. This is an issue of immense constitutional importance

to the nation and (with respect) should not be left to a few members of the judiciary to decide.

SOME FINAL COMMENTS

For the sake of completeness it is noted that there were two more related issues which were touched on, and that added weight to Justice Thomas' and Judge Beecroft's decisions:

Under the Conservation Act, people who *occupy* land adjoining a river to do require a licence or have to pay a fee in order to fish for trout from the land which they *occupy*; and

There was evidence to show that the introduction of trout had diminished the numbers of native species including eel.

In terms of the first issue Justice Thomas could not see any justification for adjoining occupiers having greater rights than Maori who hold *mana whenua* over adjoining land. on the other hand, however, this provision of the Conservation Act may also show that, if there were going to be any exceptions to the general controls over trout, those exceptions will be expressly stated in the legislation. Although it may have some 'moral' significance, the second issue does not bear directly upon the legal points at issue in this litigation. However, it may provide the basis for a claim against the Crown for interference with customary or Treaty based fishing rights.

The issues as far as trout fishing seem settled. However, the test to be applied when extinguishing Maori customary and Treaty rights will be of central importance when Maori Land Court's Marlborough Sounds Decision is appealed. That case involved customary rights to the seabed and there are a number of statutory provisions which by "necessary implication" may have restricted or even extinguished those rights. The Maori Land Court applied a test similar to that of Justice Thomas and Judge Beecroft and the question is which test will be applied by the Court on appeal?

As a final comment, clearly, Judge Beecroft, was quite correct with respect to two matters: the issue was not "clear-cut" and "value judgements" were involved.

About the author

Gerald Lanning completed a Bachelor of Law (Honours Degree) at the University of Auckland and is now a solicitor at Chapman Tripp's Auckland office. He is part of the environmental law team and has a special interest in Maori and Treaty of Waitangi issues. Previously Gerald had completed a B. Sc. in geography and a Diploma of Teaching and spent four years teaching senior physics and science.

Preparation of NZIV Guidance Notes to accompany the Institute of Chartered Accountants ED-82

In March 1998 the NZ Institute of Chartered Accountants issued an Exposure Draft (ED-82) titled Accounting for Property, Plant and Equipment. The aim of ED-82 was, if approved, to replace the present accounting standards SSAP-28 Accounting for Fixed Assets and SSAP-3 Accounting for Depreciation.

The NZIV Standards Board has been working with the NZ Institute of Chartered Accountants in commenting on ED-82 and preparing a suitable draft Guidance Note for inclusion in the NZIV's Technical Handbook. Significant progress has been made in this area but this has recently been thwarted by the International Valuers Standards Committee.

In a press release dated November 1998 they explained that the concept of "Market Value for Existing Use" (MVEU), as a basis for valuation was abruptly abandoned by the International Accounting Standards Committee. The decision came after debate on the revised International Accounting Standards, IAS 16 Property Plant and Equipment at the International Valuation Standards Committee (IVSC) held in Paris in October which is the

subject of a commentary release by the IVASC.

Philippe Malaquin, IVSC Chairman, has said "The Commentary will alert the business and financial community to the consequence of revised IAS 16. The sudden abandonment of the MVEU concept in International Accounting Standards may create confusion and lead to instability in various financial markets throughout the world. It may also force re-valuation and/or re-examination of the values currently reflected on the balance sheets of countless enterprises, entailing additional time and expense. The IVSC Management Board is seeking reaction prior to a reconsideration of International Valuation Standards in the light of the revised IAS 16."

The IVSC meetings took place at the same time as bankers and politicians gathered in Washington for the annual meetings of the International Monetary Fund and the World Bank. Over 40 valuers representing 24 countries from around the world came to Paris. IVSC extended its global reach by admitting to membership representatives from Thailand, Vietnam, Luxembourg, the Netherlands, Kazakstan.

Uzbestyan, and Macedonia.

The meeting approved *Guidance on Business Valuation* for publication. The draft document *Guidance on the Valuation of Intangible Assets* was approved for release as an exposure draft. The *Valuation of Leases and of Specialised Trading Properties*, and a draft *Glossary of Terms* are expected to be released for formal exposure following the Spring 1999 Management Board Meeting.

Philippe Malaquin said, "While those in Washington were talking of redesigning the global financial architecture, much can and still needs to be done to make capital markets safer. To quote from *"The Economist"* newspaper "Visions of a new global architecture can wait. There is work to be done."

The NZIV, through its Standards Board, is shortly to make a formal submission to the Institute of Chartered Accountants on ED-82 with regard to a few remaining outstanding issues. It is also to make a submission to the IVSC in support of the concept of "market value for the existing use."

We will keep members advised of developments in this important area of valuation.

Book Review

Property Inspection: An Appraiser's Guide

John A Simpson, M.A. I.

Published by
The Appraisal Institute
875 North Michigan Avenue
Chicago
Illinois
60611 -1980

First published by the Appraisal Institute 1997, this small and easily read text of some 98 pages is an excellent overview of the valuer's role in the appraisal and inspection of residential and commercial property, including sub-divisions, apartment buildings, shopping centres, industrial and office buildings.

Set out are six chapters headed:

- The importance of property inspection;
- Developing an inspection system;
- Inspection tools;
- Site inspection;
- Home inspection;
- Commercial property inspection;

the text clearly sets out the critical factors (obviously in an American context) that an appraiser should have regard to in undertaking property inspections.

The book opens with the comment that:-

"The importance of property inspection cannot be over-emphasised. According to data compiled by Liability Insurance Administrators, failure to disclose property defects, is one of the major reasons for errors and omissions claims against appraisers. "

And in the same chapter: "Nearly every aspect of the appraisal process is based on the property inspection skills. The traditional valuation methods - The Cost Approach, Sales Comparison Approach and Income Capitalisation Approach - are based on inspection of the subject and comparable properties. The validity of the 'Sales Comparison Approach' depends directly and critically on the inspection of the subject and comparable sales. The cost approach is based on a

physical inspection of the subject site and comparable vacant land sales, as well as comparison of the subject to cost comparables ... Other parts of the Appraisal Report, including descriptions of the site and improvements and the analysis of the subject within its market, are based on inspection skills. "

Later in the text

"In most cases, the appraiser acts as the "eyes and ears " of the client. He or she may be the only independent, impartial person involved in the property transaction. In addition to identifying important property characteristics for the reader of the appraisal, the appraisal looks for tell tale signs that a major repair may be necessary. "

Chapter one of the text, sets out clearly the reasons for property inspection as it relates to the appraisal process and to court testimony, property inspection , the relationship to financial institutions and the importance of property inspection in today's markets.

Chapter two gives important tips for developing an inspection system.

Chapter three deals with the appraiser's "tools."

Chapter four sets out, issues to be taken into account when undertaking a site inspection.

Chapter five gives the inspection processes in undertaking inspection of a residential home, while chapter six outlines the

issues involved in undertaking a series of Building Construction commercial property inspection, videos. including compliance with relevant legislation, most of John Gibson which has an equivalence in New F. N.Z.I. V Zealand Statutes.

Each chapter concludes with a succinct summary at the end of the issues raised in that chapter, and scattered throughout the text, are pertinent "appraiser's tips" which set out issues for the appraiser to consider and ways in which their particular assignment can be approached. Obviously written in an American context, the text nevertheless has valuable warnings for New Zealand Practitioners. Hints are given as to recognising and identifying materials, inherent construction faults and other issues.

As much as anything, this small and easily readable text may be regarded as economics text on the factors impacting upon property, the subject of the valuer's attention.

Heavily weighted towards residential property, 67 pages are devoted to relevant inspection techniques and supporting information. Most particularly helpful was the sample property observation check list given within the body of the text.

Priced at US \$35.00, this extremely readable text is really a must for every appraiser. It readily compliments the other texts held in the New Zealand Institute of Valuers library on property inspections, and the Institute's

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