VALUERS' JOURNAL

SEPTEMBER
1994

IN THIS ISSUE

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NEW ZEALAND VALUERS'JOURNAL

SEPTEMBER 1994 ISSUE

The NEW ZEALAND VALUERS' JOURNAL is the official publication of the New Zealand Institute of Valuers. The focus of the Journal is to publish researched articles on valuation, property investment and related matters, and to encourage the investigation and expansion of the frontiers of knowledge that cover such fields. It seeks to publish reports of decisions of hearings of tribunals, courts, and arbitrations of special relevance to the profession.
The New Zealand Institute of Valuers has a special interest in scholarly research that can be useful in property valuation and development, finance, investment, property management and market analysis, real estate and the valuation of plant. The Editorial Board is willing to work with any potential author who is developing new and exciting ideas.

Articles and correspondence for the NEW ZEALAND VALUERS' JOURNAL should be submitted to the Editor at the following address:

The Editor, NEW ZEALAND VALUERS' JOURNAL,
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All contributions should be typewritten and accompanied by a biographical note of the author. The Editor reserves the right to accept, decline or modify material. Views expressed by the editors and contributors are not necessarily endorsed by the New Zealand Institute of Valuers. Copies of manuscript should be retained by the author as they cannot be returned.

Deadline: two months prior. Each manuscript submitted will be reviewed by the Editor to evaluate its appropriateness for the Journal and assigned anonymously for review by two or more referees.
Complete editorial policy review process and style instructions are available from the editor. Business letters, subscriptions and advice of changed address should be sent to the General Secretary. The mode of citation of this volume of the NEW ZEALAND VALUERS' JOURNAL is (1994) N.Z.V.J. September page.

CONTENTS

Feature Articles

Page

EDITORIAL COMMENT

Restrictions On The Valuers' Information Highway

ollection, assimilation and dissemination of property information Cis the life-blood of valuation practice. To be effective, valuers need accurate information on the sales of properties, lease details and rentals for premises and up-to-date construction cost data.

The New Zealand Institute of Valuers has been effective for a very long period in providing nationwide property sales data, initially through periodic printed lists, then on monthly, and later fortnightly lists produced on microfiche from computer databases. Data is currently available on both microfiche and computer discs.

The NZIV has for many years also had an effective system for collection and analysis of building-cost data. Through, originally, the offices of the State Advances Corporation (later the Housing Corporation of New Zealand) and by contribution from members the information has been integrated into the very effective Modal House and Building Multiples system, developed by the NZIV to relate to most types of building structures.

The property data provided by the NZIV has never extended to rentals and premises leases data, and valuers have always been responsible for collecting and analysing this information for themselves. Valuers have extended their range of information in this field by obtaining rentals and lease details from property managers, real estate agents and property owners and by exchanging this information with other valuers. This has resulted in an effective highway of information for most valuers.

But the introduction from July last year of the Privacy Act 1993 has placed some restrictions on the collection, holding and passing on of in particular, rentals and leases information and building cost data. Fortunately, the Privacy Act will not impinge on the NZIV sales data system as this information is `public domain' that is recorded through the land transfer system and can be obtained through title searches. The Privacy Act 1993 contains twelve principles which briefly are:

1 Purpose - Personal information may not be gathered unless there is a lawful and specified purpose related to the business.

2 Source - Data must generally be collected directly from the individual concerned although there are a number of exceptions which include:

- that the information is publicly available.
- that the individual concerned authorises collection of the information from someone else.
- gathering the information would not prejudice the interests of the individual concerned.
- that the information will not be used in a form in which the individual concerned is identified.

3 Collection - The individual must be made aware of the purpose for which personal information is collected, the intended recipients, and of the rights of access to and correction of the information.

4 Manner of collection - Personal information must not be collected by an unlawful, unfair or unreasonably intrusive means.

5 Security - Personal information held must be reasonably protected against loss, unauthorised access and misuse. Where information is released the releasing agency must ensure that it is not misused

6 Access - Personal information must be available to the person to whom the information refers for checking for any necessary correction.

7 Correction - Request can be made by the individual for correction of personal information held.

8 Accuracy - Reasonable steps must be taken to ensure that before use, information is accurate, up to date, complete, relevant and not misleading.

9 Retention - Information must not be kept longer than is required for the purposes for which the information may be lawfully used.

10 Limits on Use - Personal information collected for one use may not be used for any other purpose, with a number of exceptions which include:

- the information is publicly available
- the use of the information for that other purpose is authorised by the individual concerned .
- the information is used in a form in which the individual concerned is not identified.

11 Limits on Disclosure - Personal information may not be disclosed unless there are reasonable grounds for the belief of a number of circumstances which include:

- disclosure is one of the purposes for which the information was obtained.
- the information is publicly available.
- disclosure is authorised by the individual concerned.
- disclosure is necessary to facilitate the sale of a business as a going concern.
- the information is used in such a way that the individual concerned is not identified.

12 Unique identifiers: - A unique identifier (eg code number) must not be assigned to an individual unless necessary for the agency's efficient function.

The three fundamental concepts embodied in the Privacy Act 1993 are:

- Personal information should be obtained fairly and openly with the knowledge of the person
- Personal information should be used fairly, kept up to date and be accessible to that person.
- Personal information is not to be passed on to others without the consent of that person.

In valuation practice it will be necessary for valuers to comply with the Act and it would be advisable for every valuation practice and every organisation with valuers in their employ to appoint a Privacy Officer to ensure that compliance with the Privacy Act 1993 is maintained.

It is suggested that the valuers' information highway should not be too severely restricted in the future provided that valuers ensure that they have an individual's permission for gathering, holding and disclosing personal information or that any personal information disclosed does not identify that person.

While the Privacy Act applies only to "personal information" and may not therefore relate to corporate bodies, care should be taken that any information gathered is not held or passed on in a form which may be identified as personal to individuals in the organisation involved, such as directors, shareholders or partners.

Trevor J Croot

From The President's Pen

These thoughts are being penned in mid-July, when New Plymouth is dripping with excess moisture and other parts of the country are gripped in snow and ice. In the depths of winter we all look forward to spring, with its sunshine warmth and new life cycles.

The New Zealand economy is now advancing into springtime. For the first time in over one and a half decades, the nation is not planning to bequeath ever-increasing debt levels to our grandchildren, and sound business principles are at last being applied to the majority of government spending. Private sector confidence has risen and most parts of the economy - particularly those based on production rather than consumption - are recovering from the winter of recession. Certainly, there are some clouds on the horizon for export industries struggling with the appreciating exchange rate, but there is an air of positiveness about the country which is even seeping into the main metropolitan areas.

Commercial property values appear to have `bottomed' and yield rates are now firming. Housing markets have strengthened in recent months.

The recovery will provide opportunities for the valuation profession right across the board, and hopefully stimulate increased employment for recent graduates who, as a group, have so much to offer. The Institute's marketing committee has instigated a market research survey to ascertain the public perception of valuers and those areas where members could enhance their advice and services. This research has the objectives of improving valuers earning potential, alerting our members to the opportunities that exist in the field of valuation or property advice, and improving public knowledge of the skills and expertise available within the profession.

This last objective is important it has long been my personal view that the term "valuer" does not adequately describe the range of work undertaken. Members of the Institute can be found in spheres of commerce, agribusiness, investment and savings institutions, banks, property companies, and various consultancy businesses, as well as public and private sector valuation organisations.

In fact, professionals with valuing qualifications and experience are involved across the whole range of land economy and financial services, often in executive positions.

The market researchers will have reported the survey results by the time these thoughts are published. I hope the results will become an important resource in planning future public relations and marketing strategies for the Institute, and improving public awareness of who we are and what we do.

This is essential if the profession is to participate fully in the improving and growing economy.

First Woman Appointed to Valuers Registration Board

The Minister in Charge of Valuation New Zealand, the Honourable Denis Marshall has announced a new appointment to the Valuers Registration Board and confirmed ongoing terms for two existing members. A Wellington registered public valuer and property adviser is the first woman to serve on the Valuers Registration Board. Gwendoline Daly is one of two Government appointees on the five-member Board and her term is for three years. Mr Marshall says Mrs Daly will make a significant contribution, bringing as she does, a range of skills and experience to the Board. She has worked in valuation for 14 years, including time spent working in Britain and Africa.

As a member of the Education Board of the New Zealand Institute of Valuers she is actively involved in education programmes. Mrs Daly has also presented papers on asset management and on rent reviews and lease negotiations.

Her work and contribution to the profession has been recognised in the form of the New Zealand Institute of Valuers Council Trophy for Merit.

Gwendoline Daly

Mr Marshall says he is pleased to also reappoint two members of the Valuers Registration Board for further terms. They are Mr Donn Armstrong, a public valuer and farm management consultant from Pleasant Point, and Mr Evan Gamby, a public valuer and director of the national firm of Robertson Young Telfer, in Auckland.

Valuers Registration Board New Registrar

The Valuers Registration Board has recently appointed a new Registrar who took up the position in May 1994.

Sylvia Maunder is a legal executive, and comes to the position having worked in several Wellington law firms including Bell Gully Buddle Weir and Kensington Swan.

Most recently she was employed by the New Zealand Railways Corporation and its successor, the Department of Survey and Land information, preparing the legal documentation for obtaining titles to surplus Railway's land throughout the country.

She has been active on several community and sporting organisations and is currently Secretary of the Wellington Track and Field Committee.

Amendments to Valuers Act 1948

The Valuers Act 1948 has been amended by the Valuers Amendment Act 1994, from 1 July this year, to empower the Valuers Registration Board to impose fines of up to $10,000 and to order valuers, who are the subject of disciplinary hearings, to pay costs relating to the investigation and inquiry.

An Act to amend the Valuers Act 1948 BE IT ENACTED by the Parliament of New Zealand as follows:

1. Short Title-This Act may be cited as the Valuers Amendment Act 1994. and shall be read together with and deemed part of the Valuers Act 1948 (hereinafter referred to as the principal Act).

2. Further disciplinary power of Board-(1) Section 33 of the principal Act is hereby amended by omitting from subsection (1) (as amended by section 2 (3) of the Valuers Amendment Act 1977) the expression "$1,000", and substituting the expression "$10,000".

(2) Section 33 (2) of the principal Act is hereby repealed.

3. New sections inserted-The principal Act is hereby amended by inserting, after section 33, the following sections:

"33A. Costs and expenses-In any case to which section 31 or section 33 (1) of this Act applies, the Board may order the valuer concerned to pay such sum as the Board thinks fit in respect of either or both of the following:

"(a) The costs and expenses of and incidental to the inquiry by the Board:

"(b) The costs and expenses of and incidental to the investigation conducted under section 32 of this Act in relation to the complaint to which the inquiry relates.

"33B. Enforcement of fines and order to pay costs- Every monetary penalty imposed by the Board under section 33 of this Act, and any sum ordered to be paid under section 33A of this Act, shall be recoverable as a debt due to the Board by proceedings taken by the Registrar, in the Registrar's own name, on behalf of the Board."

4. Appeals from decisions of Board-Section 34 (1) of the principal Act is hereby amended by inserting, after the word "penalty" the words "or to the payment by him of any sum under section 35A of this Act,".

Applications for Registration as a Valuer

New Interview Policy

At its meeting in June 1994, the Valuers Registration Board decided that from 1 January 1995, ALL applicants for registration as a valuer will be interviewed by the Board or a subcommittee of the Board.

Regional Locations

The Board proposes that a panel of two Board members will interview the applicants at regional locations. It is planned initially, to have the panels convene in Auckland, Wellington and Christchurch. These locations may be changed, at the Board's discretion, to other provincial centres if the number of applicants warrants an alternate venue.

Applicants may, if they wish, choose to bypass the regional panels and be interviewed by the full Board in Wellington, at their own expense.

The function of the panels is to examine and recommend to the full Board whether or not the applicant should be registered. In the event of a Decline recommendation from the panel, the applicant may, as of right, ask to be interviewed by the full Board. This will normally take place at Wellington and, again will be at the applicant's expense.

Standardised Questions

Although the membership of the panels will differ from centre to centre, it is proposed to create a library of standard questions, the salient details of which may be altered at any time by the panels, for any applicant. The questions will be reviewed and replaced from time to time. In fairness to all applicants. it is hoped, in this manner, that a uniform standard of interviews will be maintained throughout the country.

The library will contain questions on all subjects with which the Board considers applicants should be familiar. Only a selection of the standard questions will be used at any one interview. The questions for a particular applicant may be selected randomly or may pertain to the applicant's portfolio of 20 sample valuations, previously submitted to the Board.

Candidates for interviews will be asked to present themselves at a specified time and will be given thirty minutes to read the written questions and prepare themselves for interviews. Calculators will be permitted but not reference books or crib sheets.

Deadlines

Because of the increased costs involved in Board members travelling to regional locations, the interviews will take place only twice a year. It is planned to conduct the interviews in all three centres during the first week of the months of May and August.

To enable the various administrative procedures associated with applications for registration to be carried out, all applicants wishing to be interviewed in the first week of May 1995 must have their applications with the Registrar of the Valuers Registration Board by 1 February 1995. Similarly, all applicants wishing to be interviewed in the first week of August 1995 must have their applications with the Registrar by 1 May 1995.

Costs

Adopting a policy of interviewing all applicants will mean a substantial rise in the application fee paid by new applicants. It is proposed that new applicants will bear the major part of the costs, but a small portion of the increased costs will be borne by the profession.

Review

The Board plans to review the interview policy after one year's operation.

Sylvia Maunder
Registrar,Valuers Registration Board

EDITOR NEW ZEALAND VALUERS' JOURNAL

Expressions of interest are invited by the NZIV Editorial Board for the appointment as editor of the New Zealand Valuers' Journal. Enquiries and expressions of interest should be directed to the Chief Executive Officer, New Zealand Institute of Valuers at PO Box 27-146, Wellington or on telephone (04) 385 8436.

People Profiles

Ted Fitzgerald

That valuation practice has become more complex with clients demanding higher levels of performance from their professional advisers, is the opinion of Ted Fitzgerald, New Zealand Institute of Valuers (NZIV) Council member for South Canterbury.

Mr Fitzgerald, who has been an NZIV Councillor for 10 years, and is about to relinquish that position said he welcomes this trend in valuation practice because it presents fresh challenges and rewards.

From a family background on a Gisborne hill country station, farming was in his veins. In the early 1960s he "shipped off' to the South Island prior to studying at Lincoln College, (as it was known then). He successfully completed a Diploma of Valuation and Farm Management in 1966. However, by then an interest in commerce overtook any idea of a career in either agriculture or valuation.

"Five years as an executive provided me with an insight into the `real' commercial world; an experience I have since found invaluable as a practising valuer."

His interest in agriculture, flare for management and commerce, dual valuation qualifications and interests in both rural and urban valuation augmented an attitude to always try to find a better way. An interest in clients' business and property dealings left him in no doubt that a practising valuation career was for him. "In 1976 I started my Timaru-based valuation and property consultancy practice, after four years with the then Valuation Department."

During the 1980s he realised the possibilities computer technology offered, and through 1987 to 1989 he developed the electronic sales data and Valpak-2 systems now widely in use by the profession. "I believe computer technology offers immense potential and I am presently working on the development of new systems for the valuation profession", he said.

Married to Rosemary, they have two sons and one daughter, ranging in ages from 13 to 18.

Ted is a former president of the Timaru North Rotary Club, a trustee of Timaru Boys High School, and is chairman of VALGROUP, an association of 16 private valuation firms located throughout the country.

"As a profession, we must realise the great potential and rewards that education and technology can offer. We must market our knowledge and skills better if we are to avoid opportunities passing us by", he said.

Allan Ford

The New Zealand Institute of Valuers is heading in the right direction, says Allan Ford, and he thinks the Institute is starting to look seriously at what can be done, without being too restricted by existing legislation.

"We are looking constructively at directions that I am sure will be of benefit to members", he Said.

Mr Ford has been the NZIV Councillor for Waikato for two years, a position he said he finds interesting and enjoyable.

Although his firm, Ford Valuations Ltd, is based in Hamilton, he is originally from Christchurch, and like so many of his colleagues attended Lincoln College and studied for the Valuation and Farm Management Diploma.

That study involved a two-year Diploma in Agriculture followed by a one-year Valuation and Farm Management Diploma.

"I was really interested in farming but because there was no family farm to go back to, the idea of gaining registration as a valuer became my next career goal."

He joined the Government Valuation Department and was appointed to Hamilton for four years before embarking on a `couple of year's overseas experience'. On returning to New Zealand, he worked in Hamilton again before being appointed Senior Valuer in Rotorua. In 1984 he joined a valuation practice in Whakatane, and stayed there for two years before returning to Hamilton. He now has his own three-person valuation practice, specialising in urban, commercial and industrial work.

Mr Ford said the economic recovery is now affecting Waikato, and although Hamilton was hit hard by the "crash of `87", he thinks commercial and industrial property sector values have bounced back with the recovery. This became evident sooner there than in the Auckland and Wellington markets.

"We had the dairy payouts to help ease Hamilton through. When the farmers began to earn the money, they also started to spend it. That helped Hamilton."

"We have had a lot of recent low-level development. It is good sustainable development involving industrial manufacturing space initially, followed by projects such as food chains, supermarkets, and service stations." he said.

His wife Debbie has her own business, and they have four daughters, aged between two and 11. The family like to go sailing and to travel up to the Coromandel and "go bush", or to do some fishing.

"I also do a bit of running and cycling and try to keep fit. After all, it is a fairly sedentary job I am in," he said.

Change: The Key Word For Valuers

by T P Boyd

Terry Boyd is Professor of Property Studies at Lincoln University and has held lecturing positions in Australia and South Africa and also previously lectured at Lincoln University.

He is a Doctor of Philosophy, a qualification gained from Queensland University of Technology and holds a Master of Science degree in building management. He has been a practising valuer, mainly in South Africa, specialising in portfolio valuations for property unit trusts and property companies.

Introduction

New Zealand has experienced a violent property cycle over the past decade and one effect of this turbulent experience is that property investors, financiers, developers and managers are more aware of the volatility and uncertainty in property values. As a consequence, the market players are less likely to rely on their own feelings or the unsubstantiated opinion of a property professional. In-depth decision making processes are playing an increasing role in property activities and valuers can be key players in this process if they are willing to expand their current role. It is probable that the term "valuer" will not adequately describe the future role of the property professional currently referred to as the valuer or appraiser.

The need for change is not new and many valuers have written about the subject in the past. However, today the urgency is greater and the changing role of the valuer more clearly defined by the users of valuation services. In the 1960s and 1970s the Contemporary School in the USA proposed radical changes in valuation thinking.

Ratcliff spoke about a "new school" of appraisal thought, and referred to appraisal as market analysis (Ratcliff 1972 & 1975). This was the start of the period of change.

Closer to home, similar comments have been made by Jefferies (1986) in his editorial comment in the NZ Valuers' Journal, September issue.

Eight years ago he presented a vision of a possible future generation looking back on valuers and commenting that ... "The Valuers saw their traditional hold on their marketplace being eroded, but failed to see the solutions to their continued survival in diversifying to meet the multi-disciplinary demands of the emerging markets" (Jefferies 1986, p.55).

In future, the users of valuation services will require valuers to determine value in alternative market scenarios and perform more explanatory and informative roles as advisers, rather than point estimators. The changes will be examined in terms of the two major issues, namely the concept of market value and the role of the valuer.

Concept Of Market Value

Traditionally market value has been described as the price achievable between a willing buyer and a willing seller, both well informed and not under compulsion, in a normal market. In today's complex market the buyers and sellers range from long term investors to entrepreneurs, local or international, institutions or individuals, and consequently it is extremely difficult to determine who typifies the willing, well informed buyer. However, that is only part of the problem because fluctuating market conditions make it difficult to decide what represents a normal market. Hence it is necessary to be more precise on the nature of the buyer and seller and the market.

The current concept of market value is interpreted too broadly: by this I mean that market value is, at times, adjusted to take account of fairness or transactions involving some degree of compulsion while, at other times, the current market price in a distressed market is taken as the market value. It is hardly surprising that valuers arrive at different market values when the wide range of market players in a fluctuating market are considered.

Added to this is the problem that differing methodology currently being employed will result in diverse values. The days of accepting that a generalised definition of market value is sufficient guide to valuers are gone and greater clarity on the concept of market value is essential.

"...greater clarity on the concept of market value is essential."

When considering the concept of market value of real property it is important to note that there is no "intrinsic" market value of property, its value is determined by its utility.

Market value is a value in exchange, and value will relate to the demand for a property and this demand is governed by the legal and practical use that can be made of the property.

Examples can be found of properties which have no market value because of the restriction on usage (e.g. severely contaminated land). The estimation of probable use and purchaser relies heavily on a knowledge of existing markets and hence assessing market value is analysing the relevant property market and making a prediction based on the most comprehensive information available on that market. This prediction will relate to a specific property which has distinctive characteristics and hence the process applies knowledge of existing and future market trends to a particular property.

Since market analysis and its application to a specific property requires numerous subjective assumptions, it is not possible to determine a market value with certainty. It is therefore incorrect to refer to an estimate of market value as THE market value, as it is in effect the most probable market value. It is more correct

to refer to the value as the most probable figure and further elaboration of the likely range about this figure indicates that the valuer is a professional who is aware of the risks involved in the estimate. The incorporation of a range of values demonstrates the valuer's ability to critically analyse the accuracy of the uncertain variables in the calculations.

"The type of value to be determined must be precisely defined."

The type of value to be determined must be precisely defined. For instance, value determined for statutory purposes is often different from a value determined for accounting purposes, and these values are not necessarily market value.

Throughout the western world, valuers and appraisers are wrestling with the definition of different types of value. Recently, the Property Economic Task Force (1992) in Australia put forward a proposal that valuers should determine both a market value and an investment value. Unfortunately neither value was clearly defined in the report but market value was seen as a current value and investment value was a longer term value assessed from present and future cash flows. While their attempt to determine distinct value types is commendable, their proposals are difficult to implement because market value and investment value are not defined.

A more recent working paper in the USA prepared jointly by leading academics and practitioners is headed "Market Failure of Market Value Appraisals" and is a very thought-provoking article (Cooper, Brown and Swain 1993). The paper describes four distinct value types, being investment value, market value, current value and liquidation value.

Investment value is described as a long term value to a specific investor with specific investment objectives, while market value is referred to as a medium term value assuming the most probable usage in a normalised market situation (when the market is fully recovered). The current value definition establishes value under current market conditions. They state "... current value presumes current conditions represent perpetuity, just as market value presumes a normal market in perpetuity" (Cooper, Brown and Swain, 1993, p.40). Liquidation value is explained as a short term value in a forced sale situation.

These different value types define value under varying market conditions and the paper proposes methodology to assess each value type. Investment and liquidation value are readily understandable but the distinction between market and current value is not clear and the two concepts are often confused. The writer believes that valuers, at times, see market value as spanning the market value and current value scenarios described above.

The definition of market value, as opposed to other value types, requires greater clarity and the proposal of a current value for periods when the market is not normal is a possible solution. The recently agreed TIAVSC (The international Asset Value Standards Committee) definition appears to recommend a market value in a normalised market and it is uncertain to the writer whether the depressed state of the property market in New Zealand in the early nineties was considered to be a normal market within which the probable buyers and sellers were willing and not under duress. For instance, is a bank disposing of a property which it acquired as a result of payment default, a willing seller not under duress?

The Role Of The Valuer

For many years leading valuers have stressed the need for wider vision and expanded services from valuers and some valuers have taken up the challenge. The valuation profession can use the accounting profession as a model of diversification. A generation ago, accountants were merely checking figures but today provide comprehensive financial, investment, valuation and even personnel services. Valuers can similarly expand their range of services while not engaging in identical activities to accountants.

"... the role of the valuer is changing to that of a property consultant",

At the American Real Estate Society conference in Florida in May 1993, several speakers from financial institutions bluntly stated that the function of the valuer, as the provider of a single point estimate without additional information, had become obsolete. They elaborated by stating that they employed valuers to undertake comparative studies and action plans rather than provide them with a single figure which, in their opinion they were better qualified to do than the valuer. Rather than attempt to argue the merits of their opinion, it is important to accept that the clients, particularly investors, are demanding broader services from the valuer - usually for a lesser fee.

Essentially the role of the valuer is changing to that of a property consultant who is capable of advising clients on the state of the market, the comparative position of a property within the market, and various studies on the physical, legal and financial aspects of the property. Such studies require the valuer to expand into the allied fields of finance, law, investment, feasibility studies, management, property taxation and risk analysis. These services not only apply to investment property but also to owner occupied property; for instance, a person wishing to dispose of a residential property would prefer to know the state of the market, the likely marketing period and the probable price range.

The writer sees several new roles which the valuer should perform as a regular addition to the assessment of property value; among these activities are the tasks of:

- property market analysis,
- property action planning, and
- project management.

Property Market Analysis

As suggested by Ratcliff (1975, p.485) valuation is "... market analysis and nothing more." The valuer must understand the operation of the property market and make judgments in relation to a particular property. The users of valuation services are increasingly asking for explanations from valuers on how a valuation is arrived at, and valuers should see this as an opportunity for not only supplying the basis of assessment, but also providing further information on the comparative position of the subject property in the marketplace.

Fulfilling the role of a property market analyst requires that the historical data is explicitly illustrated and that this data is interpreted with specific reference to the

subject property. Hence macro-, and micro-market studies are explained and the relationship to the subject property, in terms of units of comparison, is shown. The valuer undertakes such exercises in order to determine value but seldom sells the service as part of his/her professional activity. For residential properties this might refer to the price and features of sold properties, the current state of the market and possible future trends, value factors impacting on the property, finance options and the range of the possible sale price. Investors would benefit from comparative studies of rental levels, vacancies and factors influencing the yield rate (cap rate) for the subject property.

Property Action Planning

Recommendations on the strategy to improve the return or the general performance of a property should also be a major activity for valuers. They are aware of the advantages and disadvantages of a particular property in relation to the market and are therefore well positioned to advise on plans to improve the property's performance.

Such plans may include the impact of renovations, alterations and additions. And the valuer should not hesitate to include other property professionals in such exercises. However much more than the physical framework should be examined. The leases, other contracts, impact of relevant legislation, alternative financing, ownership options, taxation and other influences on the property's performance may be incorporated in a property action plan.

The preparation of such action plans may require valuers to improve their knowledge and expertise in a particular area but this is part of the evolutionary process and an essential activity for all property professionals. Valuers should ensure that their professional associations are acting as facilitators of relevant professional development programmes so that they are able to continually expand and improve their expertise in the broadened property consulting field.

Not only are valuers in an excellent position to expand their role to incorporate market analysis and action plans, but they can also practice in the numerous, allied property service areas. The more progressive valuers are also capable of being leaders of major project analysis teams.

Project Management

Property development projects are often complex and require the services of a wide range of property professionals. Accountants, architects, attorneys, builders, engineers, financial analysts, property managers, real estate agents, valuers and others have regular and important inputs into property asset evaluation or development projects. The valuer possibly has the best overall understanding of the development and evaluation fields and is well suited to lead such projects and act in the capacity of project manager.

While accepting that valuers do occasionally perform the leadership role of property projects, this function should be promoted as a logical extension of valuation activities. Owners of major property assets, such as financial institutions, should be informed of the competency of valuers to lead a multi-disciplinary team to examine areas of development, investment, management, marketing and evaluation of real property assets.

Conclusion

The changing role of valuers requires they be aware of the breadth of value types and the differing value requirements of users of valuation services. To assume that one value is applicable in all circumstances is totally inadequate today and soon the valuer will determine many types of value. However, establishing several value figures is only the start of the changing role of valuers.

Their major task in the future will relate more explicitly to the analysis and interpretation of property markets. Their ability to provide the property owner with sound unbiased professional advice on many aspects of property development investment, valuation, management and marketing will ensure that the profession expands in the changing times ahead. Competency will be the key in the future and the valuers broad training means that they should be promoted as the logical leaders in the field of property consulting and project management.

Clearly the more extensive role of the valuer will require high levels of knowledge and expertise and a major role of the professional bodies representing property practitioners will be to offer members the opportunity to improve their current competencies.

As an indication of the changing trends, the writer obtained the impression during a recent visit to the USA that major institutional property investors were looking for proof of competency from their professional advisers rather than professional qualifications and the production of detailed mathematical analysis was often viewed with great scepticism unless supported by market evidence.

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Women In The Valuation Profession In New Zealand

by I A McCarthy

Iona McCarthy is a lecturer in valuation at Massey University. She is a registered valuer and graduated from Massey in 1980 with a BAgrSci and in 1992 with a DipBusAdmin (Distinction). She was employed as a valuer in Palmerston North before returning to a lecturing position at Massey University in 1988. Iona was awarded a Women's Suffrage Year Post Graduate Study Award by the New Zealand Institute of Valuers in 1993, and is involved in ongoing research into the Role of Women in the Valuation Profession in New Zealand.

In 1993 many New Zealander's put considerable effort into celebrating suffrage year in a wide variety of ways. While this was beneficial in highlighting the achievements of women in New Zealand it is hoped that the public's attitude to women in all roles in society will change and women will be accepted as individuals with their own expectations and aspirations for life and career.

The valuation profession in New Zealand is notably male dominated with less than 6% of current members of the New Zealand Institute of Valuers being women. The Executive Committee of the New Zealand Institute of Valuers is aware of the low representation of women in the profession and saw suffrage year as an appropriate time to address this issue. The New Zealand Institute of Valuers commissioned research into the role of women in the valuation profession after consultation with a group of women members of the Institute. This group put forward proposals for research. The results of three of the proposals are discussed in this article.

Proposal 1. To encourage women to continue further education by offering a special award for post graduate study in New Zealand or Australia.

Proposal 2. NZIV should have a women's issues portfolio.

Proposal 3. NZIV to set up a study to follow a group of women graduates over a period of time to see if women valuers progress through to middle and upper management or if they change directions and drop out. Such a study would provide useful data and the information gained would make a good basis for any affirmative action the profession might wish to make in future planning.

This article summarises the results of exploratory research into the role of women in the valuation profession in New Zealand.

The objectives of the research were:

1. To describe the employment status, pattern and productivity of all women who had been members of the New Zealand Institute of Valuers" between 1975 and 1992.
2. To describe the attitudes to and the expectations of the valuation profession, and the needs for training. employment and career development of the above group.

Research Method

The research objectives required a descriptive study of all women who had been members of the New Zealand Institute of Valuers between 1975 and 1992. The most appropriate method of data collection for this descriptive study was a mail survey designed to obtain both quantitative and attitudinal data.

Information concerning names and addresses of current and former members of the NZIV was obtained from NZIV records. The NZIV hold current membership records on computer files and were able to provide information on all current female members. Historical records of past NZIV members are stored on microfiche at the NZIV offices. These records were searched for female members. Where current addresses of past members were not available contacts within the profession were used in an attempt to locate all members of the survey group. The questionnaire was sent to 132 current female members and 36 former members, a total of 168. The questionnaire was designed to obtain information about various personal and professional characteristics of women in the valuation profession and their attitudes to the valuation profession.

Seventeen members of the survey group were unable to be contacted. Questionnaires from this group were either returned by NZ Post or by a relative. If this group is removed from the original survey group a response rate of 74.8% was achieved. Of the seventeen members of the survey group that could not be contacted, eight were current members of the NZIV and nine were former members. Response rates from former and current members were very similar.

Review Of Survey Results

This review provides first, a summary of quantitative data relating to women valuers in New Zealand. Second, the needs of women valuers for training, employment and career development are discussed. Third, survey results relating to proposals one and two (refer introduction) are given and recommendations made. Finally, other areas of importance highlighted by the survey results are discussed.

Women Valuers in New Zealand

Women valuers comprise less than 6% of current members of the NZIV and their entry to the profession has been recent. Ninety-five percent of the respondents were aged less than forty and 45% were aged less than thirty. The respondents had been employed full-time in the profession on average for only six years.

Over 90% of the respondents had attained entry to the profession with qualifications by university degree. More respondents had specialised in urban valuation than rural valuation in their university qualification (urban 57%, rural 24%, rural and urban 19%).

Student members of the NZIV were not included in the group surveyed.

Approximately 40% of the respondents had children and the majority of these were either working or considering returning to work in the valuation profession.

Of the 113 respondents, 44.2% were employed full-time in the valuation profession, 8% were employed part-time and 47.8% were not working in the valuation profession. Seventy-two percent of those not working in the profession were returning or considering returning to work in valuation.

The respondents were employed in all sectors of the profession, with Government departments and private practice being the two major employers. Very few women had attained senior/high status positions. This is, in part, a reflection of their recent entry into the profession. The women appeared to have a high degree of job stability with an average number of jobs for the survey group of two.

Income levels for those working full-time showed over 50% of the women earn less than $40,000 per annum. This information has little significance in the absence of comparative data on male valuers.

Thirteen percent of the respondents had lost interest in the profession. Due to the low age distribution it is difficult to draw conclusions from this.

Needs of women valuers for training, employment and career development

The research has highlighted the lack of training for re-entry into the profession. There are no suitable revision courses available at present. Women noted the difficulties and high cost of keeping in touch with current technology, market trends and legal changes while not working.

Women working in the profession acknowledged the importance and need for training courses and the majority spent at least one day per year on training courses. Attendance at NZIV seminars and conferences was low. The high cost of the NZIV activities was cited by some respondents as a reason for non-attendance.

The research showed that a number of women are successfully working in lfexible situations. Further research is required in this area to ensure women in these positions are not being exploited. There is a need for promotion of equitable parental leave policies and flexible employment arrangements (including part-time work and job-sharing) within both large organisations and smaller firms. As acceptance of flexible working arrangements increases it is likely that the number of women finding worthwhile careers in the area will increase.

Post graduate study award for women

The NZIV was interested to know if women members supported a special award for post graduate study to women wishing to further their education. Sixty-six percent of the survey group supported this award.

Recommendation

That a post graduate study award for women members of the NZIV be offered on an annual basis.

The award to be offered for the purposes of research or further study in the property area.

That in making the award, consideration is given to women seeking re-entry into the work force as well as those currently studying or employed.

NZIV person concerned with women's issues

The NZIV wanted to know if women members supported the employment of an NZIV person concerned with women's issues. Thirty-two percent agreed with the proposal and 34% thought it might be useful. It is believed that although this level of support is not conclusive it indicates that this position would generally be well accepted.

Recommendation

That the NZIV appoint a person to address women's issues.

The responsibilities of this position would include:

I. Provide support in cases of direct and indirect discrimination.

2. Address the employment requirements of women in terms of part-time work/ job sharing, and re-entry to the work force.

3. Initiate and maintain a women valuers network.

4. Promote valuation as a career for women within schools and universities.

5. Provide an avenue for women members of the NZIV, for dealing with complaints of sexual harassment.

6. Promote the existence and worth of female valuers to the profession.

Promotion of valuation as a career for women

The most frequently cited areas of greatest concern for women working in the profession were the low numbers of women in the profession and the lack of female representation at senior levels. To overcome this, women need to be encouraged to enrol in property degrees.

Survey results indicate that the property industry offers a range of interesting careers for women. The majority of respondents were positive about their career in valuation and would be very encouraging to any young women thinking of entering the field.

This result is of major importance in the promotion of the career to women. The respondents noted a number of benefits in choosing a career in valuation; it was seen to be an interesting and varied career providing a good balance of office and field work, it could lead into a wide range of other property related areas, has the option of self-employment, enables a woman to combine career and family and there are opportunities to work in part-time or flexible-hour positions.

This research found that the most common sources of information regarding valuation as a career were relatives, careers advisers and university staff. Industry advertising provided information to a lesser extent.

Recommendation

That the NZIV target school and university careers advisers for promotion of property courses and emphasise the benefits of this career for women.

Positive and negative aspects of employing women in the valuation profession

The respondents noted several important advantages that they had experienced as women working in the valuation profession that should be recognised by all practitioners. Namely:

- A positive reception from female clients
- Good communication skills and an ability to diffuse tense situations
- Likely to be remembered as few women work in the field
- Found less threatening by the general public
- An ability to appreciate the aesthetic aspects of property

The disadvantages experienced by the respondents while working in the valuation profession related mainly to attitudes of male colleagues within the profession. The research showed that the women experienced infrequent difficulties in all professional relationships.

Julian (1992) noted that an organisation will be better able to respond to and interact with the marketplace if its staff make-up is similar to the client commu-

nity. In 1993, in New Zealand, only 6% of current members of the New Zealand Institute of Valuers were female. This ratio is obviously quite different to the client community. Women working in the profession have identified gender advantages, and the profession as a whole must also recognise and use these advantages.

Attitude of male valuers to their female counterparts

One disappointing finding of the research was the frequently expressed existence of chauvinistic attitudes amongst male valuers. This was noted to be a problem in the workplace and at NZIV activities. One respondent noted: "Older male valuers attending NZIV functions are quite arrogant and same crack sexist jokes".

Men working within the profession should be aware of this prevalent attitude and it is hoped that they will make an effort to change!

Limitations

There were a number of limitations associated with this research. First, there was the likelihood of bias in the survey distorting the results. The main sources of bias arose from the survey group, the non-response rate and the questionnaire design.

The survey group contained only those who had been or were currently members of the NZIV. There are a large number of graduates from university property courses every year who choose not to enter the valuation profession. The reasons for these graduates not entering the profession would be numerous. They may be unable to find employment, they may have no interest in valuation. If the survey had included this group, greater in-depth information on women's attitudes to valuation as a career would have been collected. However, the sample population would have been far larger and the sampling frame would have been difficult to develop.

A further limitation of this research was that it was not comparative. It was an exploratory descriptive study of females in the valuation profession. Further research involving a longitudinal comparative study of men and women in the profession will be carried out.

Conclusions

This research was an exploratory study concerned with describing women who were members of the NZIV between 1975 and 1992. A mail survey was used to collect quantitative and attitudinal information from the women.

The research has made a considerable contribution to the literature as it is the first quantitative research to be completed in this area. Results of direct importance to the NZIV and of interest to the whole profession have been obtained.

Women have a valuable contribution to make to the profession and it is hoped that this is recognised and promoted so that the current gender imbalance improves in the future.

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The Setting Of Motel Rents

What Constitutes A Fair Rent?

by P B Nahkies

Introduction

There are an estimated 1355 motel properties in New Zealand providing 44,000 beds every evening. They are thus an important component of the New Zealand economy in general, and of the tourism industry in particular. It has been claimed that they are probably the biggest supplier of beds in the New Zealand accommodation industry. (Littlejohn 1992).

Unlike motel properties in many other countries, the typical New Zealand motel business remains an independently owned and operated business, usually run by a husband and wife team with the help of some casual staff. There has been a long-term trend of increasing complex-size, but the average is still only 12.6 units per motel complex (Littlejohn, telephone interview December 1993). The traditional New Zealand motel complex is also somewhat unusual compared with its overseas counterpart in that it usually contains full kitchen facilities.

Originally, virtually all motels in New Zealand were owned freehold with some owners employing a manager to run the business, but the majority owner-operated. Since the 1980s though, the trend has been to lease the land and buildings from an investor and for the lessee to own and operate the business. It has been estimated that approximately 70% of motels are leased in this way (Wood 1986). The main advantage of leasing is that it reduces the lessee's capital requirements and has enabled a lot of people to enter the industry who would otherwise have been excluded due to an inability to raise the capital required for a freehold property. There has been a ready market for the sale of motel leasehold businesses in which the

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This paper was presented at the Fourth Australasian Real Estate Educators Conference held at Auckland University 26-28 January 1994

purchaser buys the chattels and goodwill of the business, in addition to any lessee's interest created by favourable lease terms. Thus the prices reflect the terms of the lease which is taken over, the quality and extent of the chattels, and the profitability of the business and hence the goodwill component.

The Motel Association of New Zealand has a standard lease which it has drawn up for use by its members, but its use is far from universal in New Zealand. Although there is a wide variety of motel leases being used and a certain degree of regional variation, motel leases are generally similar in their terms. They tend to be long-term leases - usually 15 to 25 years. Rent reviews are usually at two-year intervals and generally, the lessee is responsible for all expenses. Typically, the only responsibility of the landlord is to ensure that buildings are weatherproof.

With the advent of motel leasing has come the need for setting an equitable rent between landlord and lessee. A number of different approaches have been historically adopted by valuers which I will endeavour to briefly outline along with any perceived weaknesses in the methods.

Approaches to Rent Assessment

1. Return on Capital

This method assumes that the value of the land and buildings is known and that an appropriate level of return can be established. It is often used in conjunction with a value based on a replacement cost approach. While a useful exercise to test the feasibility of new developments or as a check on other methods, it can lead to rental levels which are unobtainable if based on erroneous values for the land and buildings. This method also contradicts the principle established by David Ricardo, the 19th century economist, that values are an outcome of rent rather than rent being an outcome of value.

2. Direct Comparison.

For this method the rents for comparable complexes must be obtained and then analysed using some unit of comparison such as rent per unit, or rent per bedroom, or per bed. Typically, the results of such analysis tends to show wide variation. Results are heavily influenced by the trading performance of each complex, and in choosing comparables, attention must be paid to business performance indicators such as level of turnover, occupancy rates, tariff levels, and expenses. Differences in the standard of accommodation provided for the operator should also be considered.

3. Percentage Rents Method.

Under this method the rent is set at a certain percentage of the turnover of the motel complex, which has the effect of establishing a link between the level of rent and the financial performance of the motel business. On a philosophical level, the percentage of turnover method of setting rents has a number of disadvantages that relate to the fact that turnover is not generated solely by the rent earning assets of land and buildings, but also by the input of chattels and management of the lessee. Thus, if the turnover is increased by superior management or chattels then the landlord gets an unearned share of this increase. The reverse is also true in that if turnover is reduced due to poor management or chattels then the landlord suffers an undeserved drop in his rent.

On a more pragmatic level, the percentage turnover method suffers from the problem that turnover is at best a rude measure of the economic performance of a business as it fails to take into account the level of operating expenses of the business. It is not turnover which determines the economic viability of a business but the net operating income of the business. Any change in turnover results in a magnified change in net operating income due to the fixed nature of many of the motel expenses. Many of the expenses of the motel must be met regardless of the number of units being occupied. For example, local body taxes, accounting fees, and insurance are relatively fixed. Although many of the other expenses vary according to the occupancy of the units, such as wages and laundry charges, they often have a fixed component which in some cases is significant. Electricity and telephones fall into this category.

The impact of fixed expenses is illustrated in Exhibit 1, which compares two businesses. Property A has a low occupancy and turnover, while Property B has a high occupancy and turnover.

Exhibit 1

	Property A	Property B	Difference
Turnover	$200,000	$300,000	50%
Fixed Costs	$50,000	$50,000	0%
Variable Costs	$50,000	$62,500	25%
Total Expenses	$100,000	$112,500	12.5%
Net Operating Income	$100,000	$187,500	87.5%
Expense Ratio	50%	37.5%	

In the above example it is assumed fixed costs remain constant, while variable costs, although increasing with occupancy, do not do so in the same proportion. Note that a similar result is achieved if occupancy rates remain constant but turnover is increased by raising tariffs.

Net operating income is therefore more sensitive to changes in the fortunes of a business, but has traditionally been ignored as a reliable measure of income due to a number of inherent problems which will be discussed later in this article.

Because of its apparent simplicity, the percentage of turnover method has consistently found favour in the marketplace and is familiar to most tenants. Historically, it has been considered that a third of the turnover is an equitable amount to go towards rent, and is based on a rule-of-thumb method within the industry known as "The One Third Rule". This rule assumes that direct operating expenses will absorb one third of turnover, with the resulting two thirds residual then being split equally between the lessor and lessee. Out of the one third that goes to the lessee must come a reward for the labour put in by the lessee as well as a return on his investment.

This method has the advantage that it takes into account the operating performance of the motels and should reflect the ability of the lessee to pay. It is also simple to calculate and understand but is reliant on its underlying assumption regarding operating expenses. If expenses take up more than one-third of turnover, then the residual share to the lessee is reduced accordingly, and vice-versa. This is illustrated over page in Exhibit 2.

Exhibit 2

	Property A	Property B	Property C
Turnover	$240,000	$240,000	$240,000
Operating Expense Ratio	33.33%	50%	25%
Operating Expenses	$80,000	$120,000	$60,000
Net Operating Income	$160,000	$120,000	$180,000
less Rent	$80,000	$80,000	$80,000
Residual to Lessee	$80,000	$40,000	$100,000

The situation in New Zealand over about the last five years, for many lessee's, has been similar to that of Property B.

Expense ratios in many cases have risen to considerably more than 33.33 % and the resulting negative impact on the residual, or return to the lessee has been exacerbated by falling turnover levels. Where the lease contains a ratchet clause which has been enforced, the rents have remained at their previous levels and as a result, increased significantly relative to turnover. Thus, ratchet clauses have had the effect of breaking the link between business performance and rents, one of the advantages of a turnover-related rent.

4. Proportion of Net Operating Profit/ Net Operating Income Methods.

These methods are a refinement of the Percentage Rent Method in that they allow for expenses before distributing the resulting surplus between lessee and lessor, according to a market derived ratio. There is some debate over which expenses should be deducted before arriving at a residual. For example, should a return on and of chattels or a return to management be deducted? An example of rent assessment based on Net Income is given in an article by Gordon Jones (1989) and is shown below as Exhibit 3.

Exhibit 3

Income before expenses			$190,000
Expenses			
ACC, Accountant's Fees, Advertising.....		$75,000	
Manager's Wages		$20,000	
Return on & Recapture of Chattels			
Return	.2000		
Write-off 10 years	.0385		
Value of Chattels $100,000 @	.2385	$23,850	
			$118,850
NET INCOME			$71,150
DISTRIBUTION OF NET INCOME			
Lessee's Profit	25%	$17,787	
Lessor's Rent	75%	$53,363	
		$71,150	

My position in the debate is to support a rent based on Net Operating Income rather than the concept of a Net Income after depreciation and return on chattels as shown above. This is for a number of reasons. The first is that it is not consistent to explicitly allow for a depreciation allowance on the chattels but not make a similar allowance on the buildings. A second reason is that it locks in a return on the chattels based on a particular value and as such is like setting a rent by the "Return on Capital Approach" discussed earlier in this article. The assumed chattel value may or may not be supported by the income of the business, and the value of the chattels should reflect the income being generated. The danger is that you may have some redundant or obsolete chattels which have been overvalued but still deemed to be earning a return in the above method. The Net Income Method arrives at a Lessee's profit, which, if you ignore possible rental benefits, is synonymous with "Super Profits". Super Profits have been defined as the surplus, maintainable net profit after making an allowance for all economic resources employed, including the time, skill and effort of the proprietor and other labour employed, and for a notional return on the capital employed in the net tangible assets (Speedy, 1982). All these super profits accrue to the lessee, which is as it should be as the lessee has paid for the goodwill when purchasing the leasehold business, but it also protects these super profits at the expense of the rent to the land and buildings. In theory, these super profits are the riskiest part of the income stream, being based on the intangible asset of goodwill, and should reduce before any reduction is made to the returns to the tangible assets. One advantage of the above method is that it notionally sets aside a certain amount of income into a sinking fund for chattel replacement and prevents it from going towards rent. Unfortunately it does not prevent the same fund from being spent on servicing debt raised to pay an inflated price for the leasehold business. It is my opinion that it is excessive debt servicing requirements, as much as excessive rents, which have caused the failure of leasehold motel businesses. A solution to the problem of chattel replacement being used in some recent leases is the establishment of a compulsory maintenance fund.

Although basing rent on "Net Profit" is admirable in that it addresses the issues of business profitability and viability, and thus the ability of the tenant to pay, I consider the alternative approach illustrated in Exhibit 4 gives a better assessment of fair market rent. This approach calculates Net Operating Income ie. income before any depreciation on any assets, and before allowing for any return on chattels.

Exhibit 4

Income before expenses		$190,000
Expenses		
ACC, Accountant's Fees, Advertising.....		$75,000
Manager's Salary		$20,000
Net Operating Income		$95,000
Distribution of Net Operating Income		
Lessee's	25%	$23,750
Lessor's	75%	$71,250

This has had the effect of transferring income from the lessee to the landlord. However, if this distribution is considered inequitable, then the market derived ratio will change. For example, in order to give the tenant the same income as calculated in Exhibit 3, the distribution would be as follows:

Distribution of Net Operating Income

Lessee's	43.8%	$41,637
Lessor's	56.2%	$53,363

Another alternative is to use this general method but to base it on the concept of equal distribution contained in the One Third Rule. To do this, you would calculate Net Operating Profit before allowing any Managers salary, and split the residual equally (Bennett, 1992). This is illustrated in Exhibit 5.

Exhibit 5

Income Before Expenses	$190,000
Expenses	
ACC, Accountant's Fees, Advertising.....	$75,000
Net Operating Profit Before Management	$115,000

Distribution of Net Operating Income

Lessee	50%	$57,500
Lessor	50%	$57,500

The Role of the Industry Standard

Regardless of the particular form of Net Income/Net Operating Income approach used, a great deal of responsibility is placed on the valuer, who has the task of judging just what is an appropriate level of expenses and income for the business. Both the income and expenses should be assessed for the business on the assumption of an Average Efficient Operator. The landlord should not be penalised for a business which is being poorly run, nor should he capture the extra income generated by an exceptional operator. I believe the assumption of the average efficient operator is an important cornerstone underpinning the concept of a fair market rent for a business.

The first step in arriving at Net Operating Income, under average efficient management, is to consider the past performance of the business. A look at sets of accounts prepared for previous years is a good starting point in establishing the track record of the business, and to provide a comparison with any budgets that have been prepared.

When analysing the accounts however, the valuer needs to be aware that they were prepared for taxation purposes and therefore the operator and his accountant are usually trying to minimise the bottom line result. If these same accounts are also going to be used as the basis for rent then that is potentially adding to the temptation to manipulate the figures.

In the situation of an owner-operator who is preparing to sell his business, then the opposite problem may apply ie. he may be attempting to present an overly-flattering view of the business by inflating incomes or deflating expenses.

Thus the valuer obviously needs to consider the accuracy of income figures. Artificially high income, for example, can be caused by channelling income from other properties or businesses into the accounts of that being scrutinised. In contrast, artificially low income can result from not putting cash through the books. Similarly, the accuracy of expense figures need checking. For example, artificially high expenses can result from writing-off personal expenses against the business or concentrating expenses within a particular time period, while artificially low expenses can be achieved by deferring expenses.

There is undoubted scope in the use of `creative accounting' to manipulate the reported Net Operating Income. The valuer must therefore be in a position to judge the actual reported performance of the business against that of industry norms, and in compliance with the average efficient operator assumption. The industry standards used should be of businesses comparable to that of the business being analysed and should be used with a sound knowledge of the basis on which they were prepared and as a benchmark for comparison purposes. They should not be used as a convenient substitute for the actual business under study, as no two businesses are identical and there will undoubtedly be valid differences between the industry standard and the subject business. It is up to the valuer to recognise the reasons for the differences and consider whether adjustments to the subject can be supported. The valuer will ideally develop his own industry standards, built on a comprehensive database and thorough analysis. The result of this will be to render one-off valuations as uneconomic, and result in specialist valuers who will corner the market for valuing special-purpose properties. I see this as inevitable, and ultimately of benefit to the valuation profession. To undertake a valuation assignment on a special-purpose property requires specialist knowledge and is not a job for part-timers.

Assessing The Net Operating Income A Case Study.

In comparing the subject property with an industry standard, the valuer may well be faced with differences brought about by differing levels of tenant input, both in regards to labour, and also to chattel content. The valuer must therefore have a clear idea as to what chattels the average efficient operator will bring to the business and also what functions he will perform.

For example, will the average efficient operator own or rent his TVs, linen, telephone system, etc? If he rents them, his expenses will be higher, Net Operating Income will be lower, and so will the landlord's rent The valuer must consider what management and labour functions the average efficient operator will be expected to perform. For example, does he do his own laundry, bookwork, repairs and maintenance and gardening?

In order to answer these questions, a survey was conducted of thirteen moteliers in Christchurch, in November 1993, as a method of acquiring knowledge of local practices in the motel industry on which to base an Industry Standard. The practising specialist valuer will have built up this knowledge over some years, but for the inexperienced valuer tackling a specialist valuation assignment, considerable groundwork will be required before he is in a position to carry out his assignment with any degree of competence. In some cases he may have access to and be guided by published Industry Performance Standards such as those put out for Hotels by Ernst and Young. However, even if such material is available, it is at best a rough guide of a general nature.

In eleven of the 13 motel units surveyed, management consisted of a husband and wife team working full-time in the units and living onsite. The remaining two motels surveyed were basically run by the wife, with the husbands having outside employment. Of the thirteen, five had previously been farmers, while the rest

came from a variety of backgrounds. Eight of the thirteen managers did all their own laundry onsite, while for the other five, a laundry service was employed to wash the sheets owned by the laundry service. All chattels, including telephone systems, were owned by the businesses, with the exception of two which hired their television sets. In all cases the operators were prepared to do their own gardening, minor repairs and maintenance, while four operators were also prepared to undertake the redecoration of units.

Based on the survey results, the "Average Efficient Operator" will actually be a husband and wife team, working full-time at the motels and living onsite. They will own all the chattels involved in the business, including all linen and will do all their own laundry, basic bookkeeping, ground maintenance and minor repairs and maintenance. They would not be expected to carry out redecoration or refurbishment of units. Where a subject business differs from that of the average efficient operator, then adjustments will need to be made to the expenses. A number of other adjustments will also need to be made and examples of these are applied to a set of actual accounts in the following pages.

As a first step, the accounts for a three-year period are entered into a computer spreadsheet. An analysis for each expense item is made, both on a percentage of turnover basis, and also on a per unit basis, with a comparison showing the percentage change per year. An example of this is shown in Appendix One. This analysis highlights trends and differences between years, as well as allowing inter-firm comparison of expenses. In theory, it should be possible to analyse the financial information given, down to the individual expense level, and to check each individual expense item. In practice however, attempts to compare individual expenses were hampered by the varying classification of expenses employed by different accountants. Aggregation of different expenses was particularly troublesome.

Some of the adjustments made, will in reality, be far from black and white and may require some judicious questioning of the operator as well as comparison with other similar businesses which constitute our Industry Standard. The valuer must not lose sight of the fact that he is trying to arrive at a realistic and sustainable income for that particular business and not doing a tax audit.

The required adjustments to arrive at a Budgeted Net Operating Income are as follows:

(a) Average out any large items of "repairs and maintenance" and "replacements" or increase if necessary, to a realistic level if unusually low.

In our example set of accounts, the expenses for repairs and maintenance are both low and relatively even between years. The property is modern, in a good state of repair, which supports the low figure. But it has also been kept low due to the operator carrying out his own redecoration and maintenance programme. Based on our industry standard, repairs and maintenance should be increased to allow for this, and an adjustment is made.

(b) Eliminate mortgage interest.

In our example the amount for mortgage interest has been deducted for all years. This is a personal expense which will vary from operator to operator and is not directly related to the running of the business.

(c) Eliminate non-recurring expenses.

Into this category might fall items such as hire of plant which occurred in the first year but not the others, legal expenses and valuation fees. The questions must be asked, are these expenses directly related to the business and expected to occur each year? Would a prudent manager budget for them? A contingency sum could be included in the budget which would allow for several legitimate, but infrequently occurring items.

(d) Eliminate personal expenses.

This is a difficult one for the valuer to judge, and may include items which although allowable for tax purposes are somewhat discretionary and of limited direct benefit to the business. Into this category fall expense items such as "Entertainment" and "Travel and Conference Expenses". In the example, the amount for travelling expenses has been deducted as it relates to the operator attending a conference in another city. Security has also been disallowed as it relates to the feeding of the family dog - a poodle, whose friendly nature renders it of doubtful value as a security measure. Once again the question needs to be asked is it a necessary expense required to create and maintain the income stream of the business?

(e) Eliminate depreciation.

This is a non-cash expense which does not form part of the NOI calculation. It needs to be deducted from the expenses.

(f) Adjust for manager's salary

In the example shown, the manager's salary is not allowed for in the accounts so would be added back in as an expense if this was the basis of inter-firm comparisons. In such a case, the salary should consider the total "lifestyle" package including factors such as the size and occupancy rate of the complex, business vehicles and living accommodation provided, what duties are expected of the manager, and what living expenses are paid by the business. Information should be collected, where possible, on actual salaries being paid, though this is not always possible in an industry dominated by the owner-operator. However, traditionally within the motel industry, inter-firm comparisons have been done on the basis of an expense ratio before any management salary and this policy has been followed in the example ie. no allowance has been made for any management salary.

(g) Average out uneven expenses.

An example of this is "Printing and Stationery", which does not always occur regularly. In the example set of accounts there is a large sum in the final year when the operators had a new brochure made up, and printed more than one-year's supply of brochures. The expense for this item should therefore be adjusted to reflect the average yearly amount that would prudently be budgeted for.

(h) Adjust for differences in management input.

An adjustment has already been made to repairs and maintenance but a further adjustment could be made to "Lawn & Garden", if this expense includes the cost of labour rather than just materials. This is assuming that the "average efficient operator" does all his own gardening. In a similar way, if the example business had contracted-out laundry, then this expense would have needed to be deducted. The example contains allowances for computer software. Does the average efficient operator require this in his business, and should it be an annual expense? I have decided not to include it as an expense in my budget, but this is open to challenge and highlights the fact that the average efficient operator changes and evolves over time in response to progress and changing economics.

Preparation of the Budget.

A high degree of emphasis should be placed on factual and recorded evidence of performance where available, and the valuer should have very sound reasons for radically departing from this evidence where available. However, a problem with

accounting information prepared for tax purposes is that it often suffers from delays of over six months in its preparation. Account may need to be taken of the current performance of the business as well as general industry and economic trends. In the example, turnover has-been increased by 5% on the evidence, within the industry, of increased occupancy rates compared with the previous year, and less price discounting. For the subject, this can be checked against management records and bank statements.

Fixed Expenses have been increased by 2.5% in line with CPI inflation, while Variable Expenses have been increased 5% in line with increased occupancy. Ideally, each expense should be examined separately and adjusted as required for known cost increases or decreases.

The percentage of expenses to turnover for the Budget is 32.7% before any allowances for a management salary. This is at a lower than average level, based on the results of the survey where expenses to turnover ratios ranged from 30% to 50.4%, with an average of 41.6%. These ratios are after adjusting back to the common benchmark of average efficient management and before any management salary.

Calculation of Fair Market Rent

On the basis of the Budget shown in Appendix 3, the Fair Market Rent could be assessed as follows:

Income Before Expenses		$153,000
Expenses		$50,038
Net Operating Profit Before Management		$102,962
Distribution of Net Operating income		
Lessor	50%	$51,481
Lessee	50%	$51,481

Out of the return to the lessee of $51,481 must be paid a management salary, the balance then representing a return to the lessee on the purchase price of the leasehold business. It should be sufficient to allow for a return on and of the assets purchased, with due allowance for the risks involved in the business.

Summary.

In arriving at the rent for a special-purpose property used in a business, the onus on the valuer in arriving at a Fair Market Rent is to take cognisance of the ability of the tenant to pay this rent. In other, less specialist properties, if a rent is set beyond the ability of the tenant to pay then the expectation is that another tenant involved with a more profitable type of business will take their place. However, for a special-purpose property like a motel, raising the rent above the ability of a tenant to pay is not a sustainable option. If devices such as ratchet clauses are used to keep rents at inflated levels, then in the short-term, the property and business will not be maintained. Long-term, the tenant may go bankrupt and a new, lower, sustainable rental will need to be set to attract another tenant.

This ability to pay however is not a subjective measure applicable to the particular sitting tenant, but is an objective measure based on the concept of r' average efficient operator. In this way, a landlord is not penalised for the poor performance of his tenant nor unduly rewarded for superior tenant performance. Within the motel market, recognition of the ability to pay principle has led to the adoption of the One Third Rule. Howeve- it has been my contention in this paper that this method of turnover-based rent assessment is too crude, and the ability to pay principle needs to be better implemented by basing rent on a Net Operating Income. This would have the advantage of explicitly taking account of different expense levels amongst motel businesses. In order to arrive at a valid Net Operating Income under the average efficient operator method, a benchmark in some form of industry norm is required. Often called the "Industry Standard" this benchmark can only be established by experience and comprehensive data collection and analysis. By surve'ing 13 Motel businesses in Christchurch, I have attempted to arrive at an Industry Standard for this particular local market and to identify some of the practical difficulties inherent in the compilation of such a Standard.

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Appendix 1 - Example Of Accounts Analysis

	90/91	% TO	$/Unit	91/92	% TO	$/Unit	% Change	92/93	% TO	$/Unit	% Change
Turnover	130753	100.0%	16344	117933	100.0%	14742	-9.8%	145814	100.0%	18227	23.6%
EXPENSES											
Guest Expenses	2792	2.1%	349	4031	3.4%	504	44.4%	3375	2.3%	422	-16.3%
Accountancy	831	0.6%	104	1463	1.2%	183	76.1%	2419	1.7%	302	65.4%
Advertising	3772	2.9%	472	3781	3.2%	473	0.2%	3850	2.6%	481	1.8%
ACC	0	0.0%	0	18	0.0%	2		466	0.3%	58	2490.0%
Bad Debts	0	0.0%	0	388	0.3%	49		186	0.1%	23	-52.0%
Bank Charges	356	0.3%	45	299	0.3%	37	-16.0%	293	0.2%	37	-2.0%
Cleaning/Rubbish	1888	1.4%	236	192	0.2%	24	-89.8%	86	0.1%	11	-55.3%
Commissions Paid	59	0.0%	7	171	0.1%	21	191.5%	680	0.5%	85	297.9%
Computer Software	1295	1.0%	162	390	0.3%	49	-69.9%	384	0,3%	48	-1.4%
Credit Card Commissions	1223	0.9%	153	1796	1.5%	225	46.9%	1600	1.1%	200	-10.9%
Debt Collection	0	0.0%	0	0	0.0%	0	0.0%	15	0.0%	2	
Entertainment	0	0.0%	0	27	0.0%	3		0	0.0%	0	-100.0%

Appendix 1 Continued	90/91	% TO	$/Unit	91/92	% TO	$/Unit	% Change	92/93	% TO	$/Unit	% Change
Fees & Permits	0	0.0%	0	0	0.0%	0	0.0%	366	0.3%	46	
Freight & Cartage	0	0.0%	0	0	0.0%	0	0.0%	50	0.0%	6	-
General Expenses	1509	1.2%	189	39	0.0%	5	-97.4%	34	0.0%	4	-13.4
Hire of Plant	298	0.2%	37	0	0.0%	0	-100.0%	0	0.0%	0	-
Insurance	2557	2.0%	320	2230	1.9%	279	-12.8%	2397	1.6%	300	7.5%
Interest - Mortgage	37877	29.0%	4735	32700	27.7%	4088	-13.7%	23729	16.3%	2966	-27.4%
Land Tax	53	0.0%	7	0	0.0%	0	-100.0%	0	0.0%	0	-
Lawn & Garden	56	0.0%	7	450	0.4%	56	703.6%	507	0.3%	63	12.7%
Legal Expenses	2468	1.9%	309	38	0.0%	5	-98.5%	0	0.0%	0	-100.0%
Light, Heat & Power	4387	3.4%	548	4884	4.1%	611	11.3%	5300	3.6%	663	8.5%
Motor Vehicle Expenses	884	0.7%	111	1062	0.9%	133	20.1%	1410	1.0%	176	32.8%
Postage	192	0.1%	24	158	0.1%	20	-17.7%	181	0.1%	23	14.3%
Printing & Stationery	116	0.1%	15	388	0.3%	49	234.5%	1340	0.9%	168	245.5%
Publications & Periodicals	551	0.4%	69	795	0.7%	99	44.4%	1043	0.7%	130	31.2%
Rates	6111	4.7%	764	5392	4.6%	674	-11.8%	4467	3.1%	558	-17.1%
Repairs & Maintenance	1890	1.4%	236	3278	2.8%	410	73.4%	3995	2.7%	499	21.9%
Replacements	3005	2.3%	376	1094	0.9%	137	-63.6%	987	0.7%	123	-9.8%
Security	143	0.1%	18	197	0.2%	25	37.8%	132	0.1%	17	-33.0%
Subscriptions & Licences	1819	1.4%	227	1430	1.2%	179	-21.4%	2599	1.8%	325	81.8%
Telephone & Tolls	6348	4.9%	794	4326	3.7%	541	-31.9%	4882	3.3%	610	12.9%
Travelling Expenses	0	0.0%	0	788	0.7%	99	-	122	0.1%	15	-84.5%
Wages	1929	1.5%	241	1680	1.4%	210	-12.9%	3777	2.6%	472	124.8%
Total Expenses	84409	64.6%	10551	73485	62.3%	9186	-12.9%	70674	48.5%	8834	-3.8%
Unadjusted NOT	46345	35.4%	5793	44448	37.7%	5556	-4.1%	75140	51.5%	9393	69.1%

Appendix 2 Adjustments To Accounts

	90/91	% TO	91/92	% TO	92/93	% TO
ADJUSTMENTS						
Accountancy	0	0.0%	0	0.0%	-919	-0.6%
Cleaning/Rubbish	-1688	-1.3%	0	0.0%	0	0.0%
Computer Software	-1295	-1.0%	-390	-0.3%	-384	-0.3%
Entertainment	-27	0.0%	0	0.0%	0	0.0%
Hire of Plant	-298	-0.2%	0	0.0%	0	0.0%
Interest	-37877	-29.0%	-32700	-27.7%	-23729	-16.3%
Legal Expenses	-2468	-1.9%	-38	-0.0%	0	0.0%
Land Tax	-53	-0.0%	0	0.0%	0	0.0%
Printing & Stationery	499	0.4%	227	0.2%	0	0.0%
Repairs & Maintenance	3110	2.4%	3906	3.3%	1005	0.7%
Replacements	-1309	-1.0%	601	0.5%	708	0.5%
Security	-143	-0.1%	-197	-0.2%	-132	-0.1%
Travelling Expenses	0	0.0%	-788	-0.7%	-122	-0.1%
NET ADJUSTMENTS	-38241	-29.2%	-28989	-24.6%	-22698	-15.6%
ADJUSTED EXPENSES	46168	35.3%	44496	37.7%	47976	32.9%
ADJUSTED NOT	84586	64.7%	73437	62.3%	97838	67.1%

Appendix 3 Budget

		% TO	$/Unit
Turnover	153000	100.0%	19125
EXPENSES			
Guest Expenses	3544	2.3%	443
Accountancy	2480	1.6%	310
Advertising	4042	2.6%	505
ACC	490	0.3%	61
Bad Debts	196	0.1%	24
Bank Charges	300	0.2%	38
Cleaning/Rubbish	88	0.1%	11
Commissions Paid	714	0.5%	89
Credit Card Commissions	1680	1.1%	210
Debt Collection	16	0.0%	2
Fees & Permits	375	0.2%	47
Freight & Cartage	51	0.0%	6
General Expenses	35	0.0%	4
Insurance	2457	1.6%	307
Lawn & Garden	520	0.3%	65
Light, Heat, Power	5565	3.6%	696
Motor Vehicle Expenses	1446	0.9%	181
Postage	185	0.1%	23
Printing & Stationery	1374	0.9%	172
Publications & Periodicals	1069	0.7%	134
Rates	4579	3.0%	572
Repairs & Maintenance - General	5000	3.3%	625
Replacements	2295	1.5%	287
Subscriptions & Licences	2664	1.7%	333
Telephone & Tolls	5004	3.3%	626
Wages	3870	2.5%	484
Total Expenses	50038	32.7%	6255
NET OPERATING INCOME	102962	67.3%	12870

The Optimised Deprival Valuation Method

by B Kellett

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The topic of this paper is the Optimised Deprival approach to valuations and will discuss:

- The origin of the term.
- Traditional approaches.
- The Optimisation process.
- The Deprival rules.
- The advantages and limitations of this approach.

Origin

The term "Optimised Deprival Value" is fairly new to the valuer's vocabulary. Dr Shannon Pratt, who was the keynote speaker at the New Zealand Institute of Valuers conference in April last year, believes that the term is indigenous to New Zealand. It appears that we have `good old Kiwi ingenuity' to thank for introducing this concept. We should, therefore make sure we understand it fully.

I first came across the term when reading the methodology proposed for the valuation of TransPower in 1990. At that time the Government had started the move towards privatisation/corporatisation of public sector assets and it was found that traditional techniques were not entirely satisfactory for valuing these assets. This was because of the specialised nature of many public sector assets and the way they were funded.

Traditional Approaches

Traditional approaches to valuation are: • Comparison of sales of similar assets. • Cash flow methods.

- Depreciated cost.

Used on their own these methods have limitations:

Comparison of Sales of SimilarAssets

This method of valuation is ideal for assets such as vehicles, construction machinery, machine tools, etc which change ownership regularly. However, many assets are not normally traded on the open market and we must look at other methods for valuing these assets.

Cash Flow Methods

Competitive businesses and properties are normally valued using capitalisation of future earnings or net present value of future cash flow methodology. These methodologies are appropriate for businesses in contestable markets where external forces determine prices. However, they are not necessarily appropriate for monopolistic and publicly funded enterprises where it is difficult to establish a direct link between revenues (earnings) and costs (expenditures) for individual activities.

Depreciated Cost

Assessment of Depreciated Replacement Cost involves determining the cost of replacing existing assets with substantially identical assets and then deducting an allowance for depreciation to reflect the remaining life. It suffers from the following disadvantages:

- Technological change may allow replacement with lower-cost assets.
- Redundant assets are included at full value.
- Over-designed assets are included at full value.

The optimised deprival approach is a hybrid which incorporates techniques to overcome the limitations of these methodologies.

Optimisation

A limitation of the basic depreciated replacement cost approach is that it assumes replacement with assets substantially identical to those existing. The process of "optimisation" is an enhancement of the traditional like-with-like replacement approach that arrives at replacement costs using "modern equivalent assets" performing the same function as the existing assets. It results in an estimate of the lowest possible cost of replicating existing services using modern materials and modern technologies in the most efficient asset configuration.

- This approach takes account of technological and functional obsolescence. For example, replacement of cast-iron gas mains with polythene.
- Its use also means that current asset owners/managers/users need not be saddled with the consequences of historic decisions made by previous owners/managers. For example, over-

This paper was presented at the AGM Seminar of the Institute of Plant and Machinery Valuers held at Christchurch in April 1994.

optimistic predictions of demand may have resulted in over investment in certain locations with the result that there is now considerable under-utilised capacity in the system. Optimisation allows the system value to be based on an asset configuration that meets, but does not unduly exceed, current needs.

To apply this approach the valuer needs to determine just what form functional replacement of the assets would take. It is in this area that valuers associated with engineers and process designers (typically consulting engineers) have an advantage. The technique has been applied to natural gas utilities, electricity supply authorities and to major industries.

Deprival Value

Deprival rules provide a guide to the upper and lower limit of value and using an assessment of Discounted Cash Flow (DCF) value also gives a guide to values between these limits. If it is not possible to identify the revenue streams required for a discounted cash flow valuation, a utilisation factor can be used to judge values between the upper and lower limits. The utilisation factor will be zero for redundant assets and 100% for assets which will be fully used for the purpose they were acquired.

The first stage in assessing the deprival value is to ask the question, "Would an asset be replaced if the business were deprived of the asset?"

If the answer is:

YES - The asset is worth replacing	(Because it will generate cash flows having a DCF in excess of the replacement cost)	This represents the upper limit of Deprival Value
NO - The asset is only worth selling	(Because the proceeds from sale are greater than the DCF value)	This represents the lower limit of Deprival Value
NO - The asset is worth keeping but not replacing	(Because the asset will generate cash flows with a DCF greater than its disposal value)	The deprival value lies between the upper and lower limits

a) Upper Limit of Deprival Value

The upper limit of deprival value for assets not normally traded on the open market is the net current replacement cost. For example, the deprival value of a new asset would not be more than the replacement cost new.

b) Lower Limit of Deprival Value

The lower limit of deprival value for assets not normally traded on the open market is the net realisable value. This may be scrap value, or market value for an alternative use, less disposal costs.

c) Deprival Values Between Upper and Lower Limits

The following graphs illustrate how deprival values between the upper and lower limits can be assessed. The graph in figure 1 would be used when discounted cash flow information is available.

If discounted cash flow information is not available, a utilisation factor can be used as a substitute. The utilisation factor would be 100% if the output from the asset is at a level for which it was purchased. This assumes that the discounted cash flow at the time the asset was purchased was in excess of the cost of the asset. The use of utilisation factors is illustrated in figure 2.

FIGURE 1
(used when DCF can be assesed)

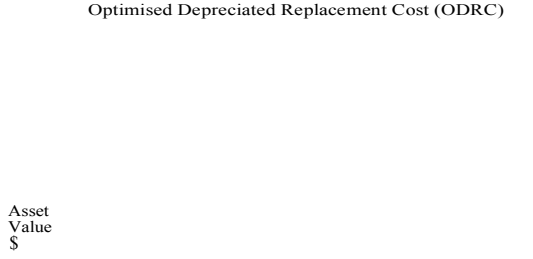
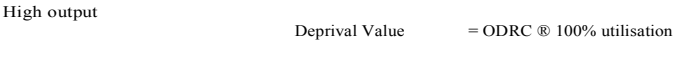


FIGURE 2
(used when DCF cannot be assesed)



Summary

1. If the cash flow approach (DCF) produces a higher value than the optimised depreciated replacement cost (ODRC), the value assigned to the assets should be the optimised depreciated replacement cost.

   This is because the firm could "replace" the assets at the lower value and would not pay more than their "net replacement cost" which is an accounting term equivalent to our ODRC.

2. If the cash flow approach DCF is lower than ODRC, the assets should be valued at the lower DCF figure.

   This is because the business cannot achieve the optimum return on the use of the assets. This inability to achieve an optimum cash return on the use of the assets could be due to external, regulatory or other external factors.

3. If the cash flow approach (DCF) produces a lower value than either ODRC or Net Realisable Value (NRV) then the cash return on the use of the assets by the firm is so low that the proper value of the assets should be set at NRV.

   This is because NRV is the lowest possible value the firm could obtain by selling in the open market for possibly an alternative use. (There may be some problems for the Valuer, deciding whether NRV should be on a collective basis, or an item by item basis).

Advantages and Limitations

The main limitation of the deprival value approach for plant and machinery is that net realisable values, depreciated replacement costs and cash flows or utilisation, needs to be determined for all the assets, or groups of assets of the firm. This entails more work than a straightforward DRC valuation or market value assessment. Another complication is that the cash flow may represent a return on factors other than "the assets", eg. goodwill, monopoly, brands.

However, the writer believes that for too long Plant and Machinery Valuers have used a single approach and as valuations become more complex (eg. when assets are transferred from public entities) there will be an increasing need for valuers to improve their valuation techniques. The deprival value approach is one way we can offer more defensible valuations.

Valuers In The Environment

by L Joyce & M Parker

Introduction

Valuers have always had a responsibility for their professional work. That covers all, aspects of a valuer's interaction with the subject matter of their valuation. But a greater emphasis is now being placed upon the way in which society as a whole relates to the environment. A headline which recently appeared in the Sydney Morning Herald would probably equally apply here in New Zealand:

> *"Most say environment more important than economy."*

Because the practice of valuation is one of continual dealing with the physical aspects of our environment, valuers will be under the spotlight.

New Zealand judges speaking of the Resource Management Act have said:

> "The RMA is informed by a wholly different environmental philosophy which places far greater emphasis on environmental protection - [it has a] strong and pervasive emphasis on avoidance of adverse effects on the environment."

This is part of a worldwide adjustment in thinking. Canadian judges have said, when speaking of Canada's environmental regulations and laws:

> *"Breaches of these regulations and laws must be dealt with in such a fashion as to prevent their repetition and to foster the principle of environmentally responsible corporate citizenship."*

The "green revolution" has added two substantial dimensions to the business of valuation. First, the effect of environment issues on the way a valuation is conducted, and second, the effect that has on valuers' professional liability. It is to this second aspect that we direct this paper: How valuers should manage the risks which arise from environmental liability.

The fact that you need to adjust your standard of care to take into account the advent of this green revolution is a classic symptom of being involved in a dynastic profession. If you will forgive the invidious comparison, your business is similar

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This paper was jointly presented by the authors at the NZIV Seminar held at Rose Park Hotel, Auckland, on 18 April 1994.

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in this respect to that of providing legal services. You have got to keep up with the latest trends to ensure that the standard you work to will protect you and your clients.

That does not mean that you should experience a rising level of paranoia about environmental responsibilities, but you should address them because we believe that, properly managed, the risk (as opposed to your awareness of this risk) should assume no greater proportions than it has before now. This may mean consideration of such things as good continuing educational procedures, contract terms which minimise your exposure, as referred to later in the paper, close interaction with associated professional disciplines, succinctly and carefully worded reports, and setting up standards for the profession which will form a minimum to which you should always have regard when conducting your business.

What are the sort of environmental problems that you might encounter in your work in New Zealand? It is interesting to look at some of the headlines which have appeared in the national newspapers within the past 12 months touching upon environmental contamination:

"MANGERE SMELL REMAINS MYSTERY"

"FUEL LEAKS SECRECY ANGERS COUNCIL"

"FARM POLLUTERS HARMING RIVERS"

"DYE IN STREAM BRINGS FINE"

"RESIDENTS PREDICT TRIPLE POLLUTING"

"COMPANY ADMITS DYEING STREAM BLUE"

"FUEL FOUND BENEATH WAREHOUSE"

"GREEN SPOTLIGHT LOOKS FOR DIRTY BACKYARDS"

"KEEPING NZ GREEN - WITH COLESLAW"

While some of those headlines are quite amusing, they highlight the many varied land uses which may be affected by contamination. The cases referred to in those media reports include septic tank seepage on residential land, oil spill into a stream running through residential land, aviation fuel leakage into clay under a carpark, agricultural waste causing contamination of farm property and adjoining local water supplies, petrol and diesel oil in the soil beneath a harbourside warehouse. The examples go on.

A report produced by Worleys Consultants in late 1992 for the Ministry of the Environment, cautiously estimated that there are about 7,800 potentially contaminated sites nationwide that would cost $620 million to clean up. The report concluded it would cost another $1,000 million to clean up those sites regarded as a moderate risk. To give you some idea of the situation, the report suggested that there were as many as 642 contaminated sites in the Wellington area alone. One can imagine that the situation in a larger business and population centre such as Auckland could mean a much higher number of contaminated sites.

Even if you treat these figures as belonging in the "guesstimate" category, there is still a very serious problem. So, when you as a valuer have a professional valuation job to do, knowing that there are these potential problems around, not knowing the history of a particular site, but keen to do a proper valuation which considers environmental impact and possible stigma, and ensure that if serious problems are present you are not fixed with liability, how do you minimise your risk?

At the centre of your concerns should be to exercise a proper standard of care when dealing with environmental matters, because that is the standard by which you will be judged if problems arise and your work is subjected to scrutiny in a claim. A very succinct statement of your position is made in an article in New Zealand Valuers' Journal for March 1994 (page 10 - by Xan Harding: "Environmental Liability and the Banker-Valuer Relationship"), Mr Harding wrote:

> *"However, a valuer's valuation has never been, and cannot be, an unequivocal statement of fact. It is merely the considered opinion of a highly trained independent professional given in good faith. A valuer has nothing to fear but his or her own negligence, measured against the objective standard of the performance of his or her peers."*

That does not mean that you need to become an environmental expert nor an environmental lawyer, perish the thought. But it does beg questions as to what is the appropriate standard; what must you be on the lookout for so that you are exercising that appropriate standard of care?

It was a feature of a very helpful series of seminars run by the New Zealand Institute of Valuers in 1992 that there was uncertainty about this area of environmental liability; about the number of contaminated sites; how the Resource Management Act would work; and, most importantly to you, how you as valuers approach the problems brought about the by greater focus on these matters.

Quite apart from techniques such as carefully considered qualifications to reports and contractual disclaimers in relation to third parties or obtaining professional indemnity insurance (which may well be limited as far as environmental contamination is concerned and is very much "the ambulance at the bottom of the cliff'), we believe that a very useful tool in managing your risk is to have a written standard against which you can measure yourselves. While the physical area of contaminated sites as a proportion of the land area of New Zealand is small, the potential liabilities arising from getting it wrong may be enormous. The risk for valuers can be exemplified where banks are involved and where large sums of money are lent in partial reliance on a valuation.

It is with this awareness in mind that we raise certain issues for consideration. These issues are raised in the context of the role played by lawyers defending valuers against claims made by their

clients and third parties in which allegations of breach of professional duty are concerned.

The Australian Institute of Valuers & Land Economists (AIVLE) have considered this issue significant enough to warrant the production of guidance notes in the form of the "Contaminated Land Practice Standard" ("the Standard") (February 1994). The Standard is provided in the form of guidance notes covering many issues on the topic which, although obviously not exhaustive, the AIVLE has considered sufficiently important that its members and those who use the service of its members should have regard to in contemplation of any contamination/ pollution matters that might affect the value of property.

The Standard is an excellent attempt to provide a comprehensive guide on environmental matters of concern for valuers and users of valuers. We use the word "attempt" with no disrespect, only because we feel sure that the AIVLE and more particularly the authors of the Standard would recognise that a standard such as this is a "living document" that needs to be updated and improved as there is more awareness of environmental contamination issues affecting property become known. It may well be that this will only occur through Court decisions involving valuers and/or changes in government and public policy brought about by experience of specific environmental/contamination issues that affect the value of property.

Nonetheless, awareness at least by AIVLE members of the matters contained in the Standard is an important step in the right direction.

It is the purpose of this paper to alert valuers about environmental issues and to have them consider the potential liability of valuers for loss and/or damage flowing from valuations of property affected by some form of contamination or pollution. This is simply a paper about

AWARENESS.

Valuers' Legal Liability

The standard of care to which a valuer is required to perform his or her legal professional duties is not static and has regard to the level of knowledge, skill and expertise of a reasonably competent member of the valuation profession judged at the relevant time. In *Singer and Friedlander v John D Wood & Co* (1977), 23 EG 212, Watkins J, noted that this standard of care requires that the average skilled valuer is:

> *"... expected to take reasonable steps to equate himself with changes and new developments affecting his skill".*

Obviously one area that has been seen as having a number of important changes and developments in recent years is that of the environment and of environmental matters that might affect the value of land. Additionally, there has been growth in environmental protection legislation. For example, the Resource Management Act 1991 has had an impact in this regard and as was stated in the discussion paper prepared by the Australian and New Zealand Environment and Conservation Council ("ANZECC") titled, *"Financial Liability for Contaminated Site Remediation"* (June 1993) at p. 65:

> *"... has changed much of the law in relation to the management of natural resources and the protection of the environment in New Zealand".*

But what will the "average skilled valuer" need to know, and against whom will that standard be compared when judging the "average skilled valuer"?

As a starting point, it seems that Courts will have regard to what the profession expects of itself and in this regard in Australia, the Standard will provide Courts with a basic guideline as to what the profession expects of itself. Therefore, in the event that a claim was made upon a valuer raising issues of that valuer's failure to have regard to contamination or pollution affecting a property, it may be that a Court will consider whether or not that valuer has at least adhered to issues raised in the Standard, in judging whether or not that valuer has breached his or her standard of care.

While a Court will not be bound by any standards set by professional bodies governing their profession (refer for example *Predith v Castle Phillips Finance Co Ltd* (1986) 2 EGLR 144 and see also *Allied Trust Bank Ltd v Edward Symons & Partners* [1993] EGCS 163), it would be strange if Courts did not consider the standards that the professions expect of themselves when seeking to determine whether there has been a breach of the standard of care by a valuer. Accordingly, it seems that this is a good reason why valuers must be aware of all relevant, available, up-to-date information, "new developments and changes" such as the very benchmarks set by their profession. Even if ultimately a Court does not judge a valuer to have been in breach of his or her duty of care by failure to comply fully or at all with a professional guideline such as the Standard, valuers would be courting danger by exhibiting a total disregard of the need to keep aware of what the profession expects of itself by any failure to be aware of professional guidelines, such as the Standard (and the further information that such documents as the Standard directs attention towards).

That is not to say that as a starting proposition the valuation profession should over-react to this issue. The environment, and the impact of contamination/pollution upon the environment, is not something that has only just arisen, albeit with a growth of world population and its demands upon limited resources, valuers of today need to have a greater awareness of the environmental issues and how they effect land, and therefore, land values. Additionally, we live in a world today where it appears that nobody ever makes a bad decision or a decision in which they concede that any loss or damage that lfows from their decision could be loss or damage that they caused themselves. Litigation against professionals, most particularly valuers (and surveyors as they are known in England), has increased to an alarming level. Valuers, like all other professionals are now being closely looked at and scrutinised in "the results" of their day-to-day practice.

How will a Court, for example, determine whether a valuer has breached his or her duty of care in proceedings brought against a valuer for professional negligence? Whilst it may be helpful to raise and consider other issues that valuers should have regard to a little later in this paper, it seems that on the current state of the law as likely to affect a valuer undertaking an inspection of property, the position of a valuer is similar to that which he or she faces in attempting to identify structural problems with the improvements on a property, when undertaking a valuation.

The Site Inspection

It has been well established that a property valuation by a valuer requires something less than a full structural building survey. Nonetheless, the valuer is expected to be able to complete an inspection that identifies potential visible structural problems, and, where his or her suspicion is aroused to "follow the trail of suspicion to its end". (See for example, *Smith v Eric S Bush; Harris & Anor v Wire Forest District Council* [1989), 2 WLR 790 and *Roberts & Anor v J Hampson & Co (a ifrm)* [1989), 2 ALL ER 504).

These decisions involved consideration of whether the valuer needed to extend the scope of his or her inspection, or in more serious cases, whether it was necessary to seek a full structural survey before undertaking the valuation.

It seems that as a starting point in relation to the visual inspection by a valuer regarding improvements, that the same principles can be applied in the area of environmental problems. Little sympathy will be obtained from a Court where a valuer undertakes an inspection of a site at such a pace as to lead to a conclusion that it was not done thoroughly, or at all.

Valuers will need to be alert to observe any abnormalities that are visually present and, further, be aware through the knowledge of potentially environmentally damaging issues, that further investigation of matters of concern or potential concern are required. As was stated in the Standard at page 4:

> *"... the member will need to complete a detailed site inspection. There are often tell-tale signs on the site that can indicate the presence of some forms of contamination. The member should look for disturbed or discoloured soils, disturbed vegetation, the presence of any chemical containers, or chemical odours, and check the quality of any surface water. In addition, the member should look for any surface soils or earthfill that may have been introduced to the site from other locations. The potential for contamination from off-site sources should also be considered."*

The Standard provides an excellent suggested environmental assessment checklist as an appendix (No.3) and although it is stated that the checklist is not intended to be exhaustive, its inclusion illustrates the type of issues that valuers should be aware of when undertaking the visual inspection of a property.

As a valuer, at least for the purpose of the visual inspection, is required to possess sufficient skills and be aware of sufficient potential (as well as actual) issues to undertake a sufficient site inspection and thereafter make or recommend the making of other enquiries to identify any potential for environmental problems - it follows from the decisions referred to above that where such a potential exists or a valuer's suspicions are aroused, the valuer will be under a duty to make further investigations and, if necessary, commission or recommend the commissioning of another expert to undertake a full environment audit so as to allow completion of the valuation report.

Awareness of publications such as the United Nations List of hazardous classes of substances, the ANZECC paper referred to, and the ANZECC paper titled *Australian and New Zealand Guidelines for the Assessment and Management of Contaminated Sites,* (January 1992) are probably a necessary complement to the site inspection. For instance, such paper gives a useful overview of relevant statutory controls (see p65 of ANZECC paper of June 1993) and also provides a framework for the assessment of what is a contaminated site, ie the ANZECC paper of January 1992 defines a contaminated site and highlights impacts to the environment from such contamination.

But, is undertaking a thorough site inspection sufficient to discharge the duty? Is seeing believing?

The answers to these questions may well be "yes", but we have some real doubts whether they are an exhaustive "yes". It may be that a visual inspection of the site, as careful and as thorough as could be undertaken, will not reveal a contaminated or polluted land use which may impact upon the value of the property. Further, it may be that failure to do more than undertake a thorough inspection will still render a valuer liable in a claim brought against him or her. The "tell-tale" signs, as referred to above may not be there, although other types of investigations may uncover "hidden" contamination or contamination from adjacent or outside sources.

As the principal author of the Standard, Mr Jeff Spencer stated in an article in "The Valuer and Land Economist" (November. 1993), titled "Standard for Valuation of Contaminated Land in Australia" at page 585:

> *"Before the preparation of the draft Standard, the difficulties experienced by property professionals in assessing contaminated property values in Australia have been widely discussed by AIVLE members. Greater media attention to certain contaminated sites focused further attention on the topic. Property professionals were particularly concerned with the difficulty in ascertaining whether or not sites contained contamination. Mere discolouration of soil, for instance, could be a hint of an "iceberg-like" situation, where significant quantities below the soil may have to be taken into account. Even if there was no evidence of contamination on the site, property professionals increasingly were expected to allow for any stigma caused by closeness to other contaminated properties."*

The concerns expressed by Mr Spencer in his article point to the very need for a greater awareness of the potential for contamination problems when valuing land, to the extent that even before the site inspection occurs, other fundamental issues should be considered.

It seems that those fundamental issues relate to the retainer and the first enquiries and investigations undertaken pursuant to that retainer.

The Retainer

At the outset, a valuer may be well advised to make sure that he or she understands the extent of their retainer and of any particular considerations arising out of that retainer that might alert them to the need to undertake specific enquiries/investigations directed at detecting potential contamination/pollution problems.

For example, instructions may be received from an industrial client seeking advice upon the value of adjoining land which may have been polluted or contaminated by the client's use of its own site, not to mention contamination or pollution caused by the current owner of the site that is to be valued.

A valuation of a multi-storey office building erected during the period when asbestos was a common building product should lead a valuer to make initial enquiries of the client as to the client's

knowledge of that asbestos, particularly if the client was the then building owner requiring a valuation for submission to a potential mortgagee.

We are aware of a firm of valuers who were instructed by a developer to value an office building which had been erected in the early 1960s, the building being the subject of a contract for sale whereby the developer was intending to refurbish and on-sell the property on a strata office floor basis. The client developer obtained a report by a consultant as to the existence of asbestos in the initial construction of the building, yet chose not to pass the report on to the valuer. Neither did the valuer enquire of the client as to whether or not the client had commissioned any separate report or had any other awareness of asbestos. Further the valuer failed to notice the extensive use of asbestos materials around lift cages, lagging to hot water pipes and in the ceiling.

After the developer client purchased the property, its profit was substantially reduced and some thought was given to suing the valuation firm for this loss. Although it was certainly arguable that the valuer had failed in his duty to his client by neglecting to observe the wide use of asbestos, and for that matter, not possessing the requisite knowledge expected of valuers valuing buildings of that particular age, not to mention the failure to enquire of the developer client's awareness of the asbestos, the matter did not proceed, primarily because the information about asbestos was already in the hands of the client.

Nonetheless, some earlier thought on the part of the valuer to consider making a request of the client as to their knowledge of asbestos, may have saved considerable concern and costs at a later time.

Accordingly, it may be that a valuer will wish to limit the scope of his or her duties in some way, and in this regard this should be made clear to the client at the outset and recorded, preferably in writing signed by the client, in the retainer. For example, and depending upon the type of property, it may be prudent to have as a term of the retainer reference to the effect that the valuer's client will, in any event. obtain a site audit or environmental impact study. Such an approach would probably be predicated upon a valuer's initial concern about the property such as in the case of a valuer valuing a known "problem" site, eg a now vacant site which was used for many years as a timber treatment plant.

By way of further example so as to confirm the previously made point about what might be considered the bare minimum requirement of a valuer's standard of care, and further considering the issue of the retainer, it is interesting to note the "Model Instructions to Valuers for Commercial and Industrial Property", as adopted by the AIVLE as a guide to the banking industry when instructing valuers. As was reported in an article in the Valuer and Land Economist (November, 1993) p. 573 Regarding the `Model" at page 575:

> *"Environmental Matters*
>
> *The existence of any past, current or potential environment hazard or contamination should be reported to the lender if identified by the valuer. If necessary the valuer should advise the requirement for an environmental audit before proceeding with the valuation. Where an adequately detailed environmental assessment report is available, the valuer should comment, if possible, on the effect of the contamination on the value and marketability of the property... The valuer should consider the property in relation to all relevant AIVLE standards."*

Those model instructions relating to what the Australian banking industry appears to require of valuers regarding environmental matters, are most instructive in that they talk about "past, current or potential environmental hazard or contamination", and it is expected of valuers that they will have considered, and as such be aware, of AIVLE standards, such as the Standard (and all that is referred to in the Standard). It should be further noted that the AIVLE introduced a "Mortgage Valuation Practice Standard" in September 1993, so as to provide guidelines as to what was expected of valuers in undertaking residential valuations for mortgage purposes. Under the heading of "Report Format" at paragraph 4.1 of the Mortgage Valuation Practice Standard, it is stated:

> *"A description of the nature of the site, its services and details of any significant observable/visual and/or known defects or hazards eg. flooding, land slip, observable or known site contamination, inadequate drainage etc.*
>
> *If the Valuer is concerned as to the possibility of site contamination at inspection he/she should where possible make all appropriate enquiries, including enquiries of the relevant statutory authority (local or otherwise) as to the history and previous use of the site and an appropriate qualification as to the result of such investigation should where necessary, be incorporated within the valuation report.*
>
> *The Valuer should indicate that he/she is not an expert in contamination issues (unless otherwise the case) where comment is made on such matters."*

It seems clear when having regard to what is now required of Australian valuers in undertaking certain valuations pursuant to instructions from the banking industry that it is a term of the retainer that those valuers be aware of all relevant AIVLE standards, thereby insisting upon valuers performing their retainer with the knowledge and awareness of all that is provided in those standards.

Knowledge of Site history and Pre/Post-Inspection Investigations

Valuers cannot rely on the fact that because the present use of a property is not environmentally hazardous they can assume that there is no danger of the land being contaminated. It is necessary to ensure that the historical land use of the site is also examined to the extent that there is no existing environmental danger or that it poses no potential environmental danger to which the client should be alerted.

The first source of information should usually be the owner of the property and those concerned with and/or owning neighbouring properties. Such inquiries alone will not, however, usually be sufficient unless a clear understanding of a potential problem arises from those investigations. As is stated at paragraph 3.1 of the Standard:

> *"Previous owners and employees can be a good source of information on the property's history. Local councils can provide a wealth of information on more prominent properties, and a search of titles can provide some indication of former use. Many State*

Governments have aerial photographs that can assist in identifying some former uses. Government departments such as those involved with mining, public water supply, environment and health, may have regulating records and other useful information."

Where such information is available, the valuer should trace the historical land use as far as possible, record all prior land uses, and carefully consider their potential environmental impact. Although the Standard sets out these requirements for Australian valuers, we can see no reason why there would be any different requirement for valuers in New Zealand.

Where such records are not readily available or the cost or delay in obtaining such records makes this task impractical, the valuer should ensure that the valuation is made subject to a clear and precise qualification recommending that further investigation is made and offering to review the valuation once such information is available.

Once alerted that a past proprietor may have had a land use and/or reputation for engaging in environmentally hazardous activities, or whose company name discloses the type of land use of a particular property, a valuer should try and conclude through further investigation that there was, or is, or maybe there has been, contamination or pollution of the subject property. Those investigations whether concluded or not should be covered thoroughly in the report to the client.

In an article by Mr R R Nathans, titled "Additional Risks for Valuers" (the Valuer and Land Economist, February 1993, 363 at 366-367) Mr Nathan discusses the investigations as to site history. At page 367, he says:

"In this regard, valuers now need to go back as far as council or other statutory records will permit to investigate and to carefully log all previous land uses. If municipal records indicate an existing industrial or related use of the site at the time local record-keeping began, and such use may have had the potential to contaminate, it may in certain circumstances be necessary to make searches of other Government archives (for example, the Land Titles Office) to establish the full history of the site, if necessary, back to the Crown Grant... In any event, a search of all predecessors in title can be handy because identification by name or previous owners often can give handy clues as to previous land use, either simply by reference to the name, for example, APC Paint Manufacturing Pty Limited, or to reputation."

In addition to making enquiries as to the property's prior land use, it is prudent to enquire about current and previous land use of neighbouring and adjoining properties. Often one polluting site may contaminate nearby and adjoining properties and vice versa. Aerial photographs that are kept in municipal and council records may reveal likely problems from neighbouring properties. An example of this may be where a valuer is valuing an industrial property situated adjacent to a particular smelter operation which emits certain contaminants.

It may even be that enquiries of an appropriate authority will reveal a past breach of environmental legislation, so as to alert a valuer to the fact that the property has been polluted or contaminated in some way (and may still be contaminated even if the [then] owner has been prosecuted) even if the initial pollution and/or contamination has ceased and (allegedly) been cleaned up. In any event, alert the reader of the valuation report to the need for a check of the property.

This raises the general issue of the need for valuers to be aware of particular legislation that either provides assistance and direction as to likely contamination and/or pollution, or alternatively, legislation which raises requirements that will affect the value of land through the operation of that legislation whereby a restriction applies to the property.

In certain Australian States, environmental protection authorities have begun to compile registers of contaminated sites. It is our understanding that these registers are not complete at this time. In addition, the Environmental Protection Authority in another State keeps an informal register of contaminated sites although the register is not required by legislation, nor is the recording of properties on the register, compulsory. When such registers are available to valuers in New Zealand, then it would be worthwhile considering a search of the register, particularly if the valuer has some cause for concern. If a client initially limits the valuer's instructions, it would be strongly recommended that a suitably worded qualification to the effect that "a search of the register (or other statutory records) should be undertaken" be added to the report.

The Valuation Report

Every valuation report should, as a matter of course, contain a suitable qualification regarding environmental liability and, in particular, it should cite the limited extent of the investigations carried out. As always, the qualification clause should reflect the scope of the valuer's duty as agreed with the client and formalised in the initial retainer or any subsequent modification of that retainer. Of course, incorporation of such a qualification cannot be expected to override a situation where the valuer was aware of or ought to have been aware of an environmental problem, but did not report upon the problem and its impact on value.

The following qualifications may be suitable where the valuer's investigation and site inspection reveal no evidence of environmental problems. They are hypothetical examples of qualifications that may apply. They are not exhaustive examples and it is recommended valuers consider each situation to be covered and the words needed to express the valuer's position.

"A site inspection has not revealed any obvious pollution or contamination. Therefore, this valuation has been prepared on the basis that the site is not contaminated and has not been affected by pollutants of any kind. Any contamination of the land or existence of pollutants on the land is likely to affect the value of the land. Verification that the property is free from contamination and has not been affected by pollutants of any kind should be obtained from a suitably qualified environmental consultant. Should subsequent investigation show that the site is contaminated, our valuation will require revision." "The site has been used for residential purposes for at least "x" years (a considerable period).

We are not experts in identifying environmental hazards, but our inspection of the site did not reveal any contamination or pollution

affectation. However, we would recommend that a check be made with an environmental consultant. Should subsequent investigation show that the site is contaminated, our valuation will require revision.

Our enquiries at the local Council indicate that the site is not recorded as having previously been used for an industrial manufacturing use or for the storage (either above ground or underground) of any chemical substance. Our enquiries indicate that the Environmental Planning Authority is unaware of the existence of any site contamination. Whilst our inspection of the site surface confirms the result of those enquiries, we have not investigated the site beneath the surface or undertaken vegetation, ground water or soil sampling. This valuation is therefore subject to a satisfactory contaminated site assessment report from environmental consultants."

Reference should also be made to further examples of qualification clauses contained within the Standard. It is emphasised again that valuers should not just adopt a predetermined qualification clause; there being no such thing as a "clause for all occasions".

Where the valuer reaches the conclusion, based upon his or her investigation and site inspection, that there may exist potential or actual environmental problems, then the valuer will be required to follow that "trail of suspicion" to its end or make a strong recommendation that some other expert be retained before completion of the valuation. Refer to *Smith v Eric S Bush, Roberts v Hampson,* mentioned earlier in this paper. As the environment is quite a specialised area, the valuer will not normally be suitably qualified to go beyond the initial detection of environmental problems. Therefore this "follow-up" will involve a recommendation being made to the client that a full environmental audit be obtained from a suitably qualified expert. Where the client accepts the valuers advice and obtains an environmental audit the valuer should, where possible, postpone the completion of his or her report until the audit results are available. These results should be considered closely in determining the property value and should in all cases be explicitly referred to in the valuation report. Alternatively, the valuer may complete the valuation before the environmental audit is undertaken. Where this latter course is followed, the valuation report should refer to the factors that reveal the likelihood of environmental problems, state clearly that the valuer is not an expert in environmental matters and that the valuation given is made subject to the making of a full environmental audit. The valuation should be made on the basis that upon receipt of the environmental audit the valuation should be resubmitted to the valuer for review. Where the client decides, against the valuers advice, not to obtain an environmental audit, the valuer must consider carefully whether he or she should make any valuation. This decision will depend upon the likelihood of contamination and the apparent extent of contamination. It is submitted that the valuer may continue with the valuation in most cases, provided that great care is taken and the valuer makes it quite clear that he/she is completing the valuation on this basis and that the valuation is strongly qualified to reflect the particular instructions. In particular, the valuer should only proceed after ensuring that specific written instructions, signed by the client, are received. These instructions should state that the valuer has advised the client to seek a full environmental audit, together with the reasons for that advice, and a statement, that despite this advice, the client wishes the valuer to proceed with the valuation on the understanding that the valuer accepts no liability for any environmental problems as they affect value. In addition, the valuation report given in pursuance of these instructions should contain full details of any evidence of potential environmental problems revealed by the valuer, a strong disclaimer stating that the valuer is not an environmental expert and accepts no liability for any loss arising from the environmental condition of the property, and a recital of the circumstances in which the valuer advised that an expert environmental audit be carried out. Such an exercise, is therefore, an exercise in risk transfer. That is, the client (and also third parties) understands who is accepting the risk by having the valuer complete his/her valuation on that basis. The following qualifications illustrate the type of information that should be identified in a valuation report where the valuer's investigation and inspection reveal some evidence of contamination. These are obviously only hypothetical examples and are not exhaustive in terms of what might be appropriate.

"From our inspection of the property we consider that there is the potential for (detail past and/or current contamination) to exist and would recommend that an environmental audit be undertaken. Please note that our valuation has been assessed on the basis of no onsite contamination. Should the abovementioned audit reveal any contamination, our valuation will require revision."

"The site is (or has been) occupied by (insert details) which, having regard to the nature of the site use (eg processing of chemicals used or stored) has a potential to cause (soil) contamination. Our enquiries indicate that the Environmental Planning Authority is unaware of any contamination, however, we recommend that an inspection be undertaken by (details of experts) to reveal any contamination, and if so, our valuation will require revision."

"The site (has been used for) (adjoins a site) which (has been, is) used for an industry which can cause environmental pollution (provide details). Our inspection of the site did not reveal any contamination, however, as we are not experts in identifying environmental hazards, we recommend that an environmental consultant be engaged to confirm that the site is not contaminated."

"Consequently, our valuation is on the basis that the site is not contaminated and if subsequent investigation shows the site to be contaminated, our valuation will require revision."

"Our inspection of the site revealed (oil or similar industrial filling, etc) which may be an environmental pollutant."

"We recommend that an environmental consultant should be engaged to inspect and report on the site."

"Our valuation is on the basis of an environmental consultant confirming that the abovementioned possible contamination does not affect the property and does not require costly removal or site treatment. If the consultant's report indicates costly removal or site treatment is necessary, our valuation will require revision."

Cleaning Up the Mess!

If it wasn't enough for valuers to be concerned about being held liable for their failure to detect and report upon potential or actual contamination/pollution, then it is possible that a liability could arise in the way in which a valuer reports upon such contamination or pollution and its concomitant effect on value.

Obviously, land that is contaminated or polluted or adjacent to contaminated or polluted land, will generally be worth less than land not so affected. It is not the purpose of this paper to attempt to undertake the valuer's role in assessing the effect or impact on value caused by such contamination or pollution.

Nonetheless, it may be that a further liability arises when valuers advise upon the "cleaning up of the mess", when such advice fads short of what is required to do so and as such has an overall impact upon value.

As Mr Nathans states in his excellent article, op cit, at page 368:

> *"If you discover land degradation or land in such state of contamination that it requires remediation, value the land in accordance with your retainer. Value it as you find it without making uneducated assumptions about the costs of rectification or remediation. If your experience does not allow you to deal with environmental matters or you do not have the expertise to estimate costs of remediation, you have a duty to make the appropriate qualification recommending further investigation. Failing to do so may amount to negligence."*

Although Mr Nathans then further suggests that it may be incumbent upon a valuer to provide, from time to time, costs of carrying out works required by certain authorities, it is submitted that the better position for valuers to take is to, firstly, attempt to assess the impact on value of certain contamination and, if possible, the remediation work needed for correction, but only to do so by adopting and following valuation principles which are known to valuers and are within the expertise of the valuers. *To do* otherwise may place a valuer outside his or her expertise.

Secondly, if it is not possible nor within the expertise and experience of a valuer to provide an assessment of impact of such contamination and/or pollution, and any remediation required, then as Mr Nathans quite properly states, a strong recommendation and/or appropriately worded disclaimer/qualification should be inserted in the valuation report, along with a recommendation that the valuer provide further verbal endorsement to the client of the view set out in the report.

Summary

The recent expansion in the significance of potential environmental problems and the proliferation of environmental protection legislation in New Zealand, Australia and elsewhere, has had a reasonably significant effect upon the valuation profession. It is vitally important that all valuers keep abreast of these changes. Failure by a valuer to be aware of the environmental aspects of the property being valued may result in significant liability. This area is of particular concern to valuers because while it is not a relatively new area of consideration in valuation practice (save for the increase in legislation), it requires the valuer to alter past, entrenched valuation procedures to include consideration of potential environmental problems. Finally, it is of particular concern because of the large losses that may be incurred by a client or third party either as a direct consequence of the contamination or as a result of the environmental protection legislation. Such losses of course may be sought to be offset by a claim against a valuer who has reported on and valued the property. The potential magnitude of those losses may also well exceed the limit of indemnity that a valuer has under his/her professional indemnity policy.

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The Regulation Of Contaminated Land

by N Hemmings

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1. Introduction

Protection of the environment was not recognised as a significant political issue until about 1970 when the USA adopted the National Environmental Policy (NEPAL). Global concern was highlighted by the United Nations in the 1972 Stockholm Declaration; viz:

> *"Man has the fundamental right to freedom, equality and adequate conditions of life, and an environment of a quality that permits a life of dignity and well-being".*

Environmental control is now a matter of major community concern and in most developed countries environmental issues no longer take second place to economic and industrial development.

Whilst environmental control legislation has been in force in all States of Australia for many years, the environment and the nature and scope of control of pollution continues to be a matter of constant and intense debate.

As a consequence of political reactions to community pressure the last decade has seen a plethora of comprehensive and hard-hitting legislation in Australia, with the emphasis upon a new range of environmental crimes to control activities which are likely to affect the environment.

New South Wales has led in such areas, followed by Victoria and Queensland, and most other States are likely to follow. Environmental laws impose heavy penalties on activities which cause pollution or are likely to harm the environment. Such liability to to such fines extends not only to users and occupiers of land, but to the owner of the waste or the person who caused the contamination. Clean-up obligations and costs may be imposed even after disposal of the land and the termination of the activities.

Environmental issues now have a most efficient and increasingly important impact upon the development and use of land and upon land value. Failure to recognise and consider such matters have exposed valuers and land managers to significant negligence claims.

Land use now requires a wide range of approvals and licences. Most legislation now also seeks to make even statutory authorities who use or permit others to use public land to be environmentally sensitive' in the grant of any approval to carry out the activity.

However, the trend is now away from solely a "control and command" approach which only punishes after pollution, to civil enforcement and strategies which will compel private sector enforcement. The trend is to create or consolidate State and Federal environmental protection authorities with big budgets and wide powers. Such agencies are liable to enforce the new legislation, with less emphasis on punishment and are likely to impose and encourage economic incentives upon industry to improve or protect the environment. Compliance with environmental responsibilities is increasingly being enforced by groups other than regulatory authorities.

To avoid accepting liability, financial institutions and parties to the sale or lease of land have been compelled to assume a role in environmental monitoring. Corporations now, as a matter of course introduce comprehensive due diligence programmes to protect directors or managers from prosecution.

This paper will discuss these changes and trends in environmental control, problems arising therefrom and effect upon land use and its value.

2. International Environmental Problems

International conferences have identified the following as major influences upon the world environment:

(a) World climate change induced by greenhouse gases;

(b) Increased pollution and toxification of air and water;

(c) Destruction of the stratospheric ozone layer; and

(d) Desertification of terrestrial and aquatic ecosystems.

These factors give rise to the following problems, some of which are unlikely to have an effect upon the value of land in the short term:

I e.g. Part 5 of Environmental Planning Assessment Act (NSW) 1979.

This paper was presented as the Keynote address at the NZIV Seminar held at the Rose Park Hotel, Auckland, on 18 April 1994.

(i) Sea Level Change

It is claimed that sea level has risen by ten to 20 centimetres over the last century and predicted to accelerate to 30-50 centimetres by 2050. If this actually happens it will, in the long term, threaten low islands and coastal zones and make some island countries uninhabitable. Land usage and values in coastal areas will at some stage alter significantly.

(ii) Water Resources

Water availability in areas of marginal precipitation are predicted to decrease in the long term.

(iii) Forestry

Forests which are sensitive to warmer temperatures are predicted to be reduced at some future time. Changes in precipitation are also likely to reduce forest areas.

(iv) Deforestation

Whilst deforestation is mainly an activity in the temperate latitudes, it is now carried out on an increasing scale in the tropics. It is also a long term problem which increases the atmospheric concentration of change. Deforestation contributes to a wide range of environmental damage by way of increase of erosion of soils, a reduction in the capacity of soils to hold water and an increased likelihood and severity of floods.

(v) Land Degradation and Polluted Discharges

This is an immediate and increasing problem affecting land value. The main causes of land degradation and polluted discharges are said to be:

(a) acidification caused by emission of fossil fuels;

(b) increased runoff of precipitation and flooding caused by deforestation, water-logging and salinisation;

(c) increased use of marginal land for agricultural production;

(d) rapid increase in world population, particularly in the developing world - since 1950, world population has increased from 2.5 billion to about 5 billion people and expected to double again before the middle of the next century;

(e) increased use of chemicals and other polluting substances, particularly in industry and agriculture.

Initially regulatory authorities in Australia were substantially influenced by the nature and scope of environmental control legislation and practices in Europe, but most of all by the USA' where CERCLA imposed strict joint and several retrospective liability on polluters. Public pressure has influenced governments to introduce similar legislation in Australia, but not yet as onerous. In the USA a person with any degree of responsibility was made liable for the entire cost of restoring a site. CERCLA was supplemented by legislation which imposed `cradle to grave' responsibility for the handling hazardous waste.'

To date, whilst Australian governments are concerned with the likely long term environmental problems, they have resorted mainly to issues related to pollution of air and water and land degradation.

Public pressure upon politicians and public concern for the environment has been highlighted by the results of a number of surveys. In a survey into public concern as to major crimes, environmental pollution was nominated as the third-most serious crime. Surprisingly many serious crimes were regarded as being of less significance.

Many industries are now most conscious of a bad public image and the chemical industry was unpleasantly surprised by survey results from residents in Australia's five capital cities. That 1992 survey[4] revealed that whilst 90% surveyed had little or no knowledge of the chemical industry 75% were nevertheless concerned with the operation of the chemical industry. Of most concern was that the public generally believed that the industry is associated with danger from pollution and health, is involved in secrecy, dishonesty and lack of ethics.

Politicians continue to respond to such public concern for the environment by creating more environmental crimes with ever-increasing, substantial, penalties and wide-ranging liability for clean up costs. This is usually described as a "command and control" system. Regularly, experience has shown that such approaches have limited success other than to punish acts of pollution.

That system has community support because, by creating new offences with heavy penalties and regular prosecutions, politicians are seen to be protecting the environment. Unfortunately, this is a false perception and punishment does not usually prevent or abate pollution. Nevertheless, this type of legislation will always remain because it is inevitable that an effective environmental control regime be backed by command and control legislation to punish acts of pollution. However, in recent years the trend has increasingly been to rely more on civil enforcement of control obligations and prevent pollution and to adopt strategies to encourage private sector induced environmental monitoring and control practices.

3. Structure of Government in Australia

Unfortunately, many strategies to encourage private sector control cannot be enforced by law because Australia does not possess comprehensive or uniform national legislation to protect the environment.

The Commonwealth of Australia is a federation with three tiers of government, namely Federal, State and Local. The power of the Federal Parliament is dictated by the Australian Constitution. There is no specific power in the Constitution which gives the Federal Parliament the power to make laws with regard to the environment. Hence, historically, environmental legislation has emanated from the State Parliaments. Increasingly, however, there is pressure upon the Federal Government to use its constitutional power over trading corporations, trade and commerce and external affairs to make laws with respect to environmental protection.

At the United National Conference on Environment and Development, held in Brazil in June 1992, Australia committed us to the Conference objectives. When implemented, recommended controls will probably have a most significant impact upon industry, particularly mining and heavy industry.

[2] cf. Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) commonly known as "Superfund".

Resource Conservation and Recovery Act.

[°] UNIDO conference Melbourne, 7 October 1993.

(Continues on Page 37)

LEGAL ISSUES

Companies Act Reform

D Quigg & R O'Neill

A. Introduction

The Companies Act 1993 ("the 1993 Act") came into effect on 1 July 1994. The 1993 Act will impact on all valuers that are either incorporated as companies, or where valuers provide their services to clients that are companies.

It is therefore imperative for all valuers at the very least to be aware of the new reforms, so that they can make informed decisions and gain the best possible commercial advantage in respect of both the valuer's own company, and providing/ expanding service to client companies.

This article is divided as follows;

- A general overview of the reforms introduced by the 1993 Act;
- A summary of the advantages and disadvantages of re-registration under the 1993 Act;
- Areas in which a valuers' company clients may seek valuers' advice as a result of the 1993 Act (and therefore create marketing opportunities for valuers).

B. Overview of Reforms

Immediate Changes

Immediate changes to the existing Companies Act 1955 became effective on I July 1994. Whether a company is registered under the 1955 Act or the 1993 Act a number of the reforms introduced by the 1993 Act already apply. Some of these are as follows;

Directors' duties and liabilities: Fundamental reform of directors' duties, powers and liabilities has increased the standard of responsibility required of directors significantly.

Shareholders' rights: Greater enforceability of the new directors' duties is given to shareholders through the use of, for example, "derivative actions" by shareholders. A "derivative action" is the ability of a shareholder (or a director) to bring an action in the name of the company and at the cost of the company. The shareholders are also given easier access to more powerful rights to obtain information in respect of the company, which will further increase the ability for shareholders to enforce directors' duties. This will result in a greater risk of directors having personal claims being made against directors.

Directors of subsidiaries: Directors of subsidiaries and joint venture companies are able to act in the best interests of the parent company or appointing shareholder, if expressly provided for in the Company's constitution. This is particularly useful in group company situations where, for example, a director of a subsidiary company is able to act in the best interests of the parent company, rather than having to act solely in the best interests of the subsidiary company.

Directors' and officers' liability indemnity insurance: Perhaps as a result of the increase in the exposure of directors to liabilities, the legislators have widened the ability for the company to provide insurance and indemnity for directors and employees.

Name protection: A new company name approval regime will also apply immediately. As a result, only applications to the Companies Office for approvals of names identical or almost identical to existing companies will be refused by the Registrar of Companies. The legislators have decided that the commercial community will need to bring actions for breach of trade names and trade marks under the Fair Trading Act or for common law passing off, in order to defeat rival parties wishing to benefit from another's goodwill.

Amalgamations: A new procedure known as an "amalgamation" has been made available to companies. Although this procedure will be useful in the merger of unrelated parties, the use of the amalgamation procedure is most effective as a time and cost- efficient alternative method to winding up unwanted companies in a group of companies. Instead of having to transfer the assets of the unwanted company to another group company (thus requiring the consents of landlords, lessors and contractors), the assets and liabilities

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of the amalgamating company vest in the amalgamated company.

No common seal: Subject to the requirements of the Act, the requirements in respect of the execution of documents by companies has been reformed to allow companies to execute documents without having to affix the common seal. However, companies may continue to use the common seal if provided for in the constitution.

Reforms affecting companies under the 1993 Act only

Companies that are either incorporated after 1 July 1994, or are re-registered under the 1993 Act are subject to the following reforms;

Capital maintenance rules relaxed: The existing "capital maintenance rules" which have previously dominated company law in New Zealand have been relaxed. This involves the abolition of concepts such as par value of shares and nominal capital, which have been replaced by permitting a company to buy its own shares, and greater freedom in the financing of the acquisition of its shares, subject to statutory protection for shareholders and creditors.

Public/private distinction gone: The distinction between a private company and a public company is abolished. Previously, any company that had more than seven shareholders was required to be incorporated as a public company, and accordingly had to undertake the expense of having their accounts audited and subjecting their financial accounts to public analysis by filing their accounts at the Companies Office. Under the 1993 Act, only companies that are Issuers or subsidiaries of overseas companies are required to have the accounts audited and filed at the Companies Office.

Solvency test: There is a general prohibition on companies making "distributions" unless the directors believe that the company can satisfy a statutory solvency test immediately after the distribution. The solvency test comprises two parts, a liquidity test whereby the company must be able to pay its debts as they become due in the normal course of business, and a balance sheet test whereby the value of a company's total assets must be greater than the value of its total liabilities (including contingent liabilities) immediately after the distribution is made. It should be noted that the definition of a "distribution" is very widely cast under the 1993 Act. The definition includes the payment of a dividend by the company, but is wide enough to also include, for example, the payment of excessive salaries to shareholders which are intended payments to avoid the payment of a dividend.

Major transaction: The entering into of a "major transaction" requires approval by special resolution of the shareholders of the company. A "major transaction" is the acquisition or disposition of assets or the incurring of liabilities equivalent to the greater part of the company's assets.

Compulsory minority buyout: There are provisions allowing "dissenting shareholders" to require the company to compulsorily purchase their shares in certain circumstances. A "dissenting shareholder" is any shareholder who votes against certain resolutions (e.g. a major transaction) passed by the majority shareholders.

Constitution: Although the 1993 Act does not require a company to have a constitution (a constitution is similar to a Company's Articles of Association under the 1955 Act) it is likely that most companies will, in any event, require a constitution to take advantage of the added flexibilities provided by the 1993 Act (e.g. share buyback rights) and to ensure that both existing unique shareholders' rights and unique existing company procedures continue to be provided for.

C. Re-Registration

When is the best time?

As most people are now aware, existing companies are required to re-register under the 1993 Act during the period I July 1994 to 1 July 1997.

Because companies have three years within which to re-register, they need to ensure that maximum benefit is derived from the timing of re-registration. It is therefore a process of balancing the advantages of re-registration against the disadvantages of re-registration. This will enable the directors to decide whether it is commercially advantageous to re-register early, or whether the disadvantages of re-registration will result in the decision to re-register being left to a later date. Unfortunately, there is no general rule as to the best time to re-register. We have already advised some corporate clients (large and small) that they should re-register under the 1993 Act immediately, and other corporate clients that they should delay re-registration for as long as possible. From our experience therefore, there is a danger in taking a global approach in relation to re-registration. It is advisable to seek legal advice so that a specific recommendation can be made based on the circumstances of each company.

Until an existing company re-registers, it continues to be governed by the 1955 Act. However, as indicated above, a number of amendments have been made to both the 1993 Act and the 1955 Act. For example, the widened directors' duties, powers and obligations, enhanced shareholders' rights and simplified amalgamation procedures all apply to a company whether it re-registers or not. Therefore, these matters will play no part in the decision on the timing of re-registration.

If a company is uncomfortable with the reforms, and in particular the enhanced directors' duties, consideration should be given to whether a company structure is in fact the most appropriate vehicle with which to operate a valuation business. The increase in personal liability on directors, not just in the area of corporate law but also in respect of, for example, the Resource Management Act and the Building Act, together with the requirement for directors to give personal guarantees in respect of business obligations, have to a large extent eroded the "corporate veil" protection that many company proprietors believe is available to them. It may be that partnerships, trading trustees, or sole trading ventures are valid alternatives.

Although it is impossible to generalise, the advantages and disadvantages of re-registration can be categorised as follows:

Advantages of Re-registration

Advantages of early re-registration include;

Avoid changing Articles of Association: The ability to take advantage of some of the reforms immediately without having to first change the Articles of Association, and then at a later date re-register the company. This will save both time and money. Important reforms that require a change to the Articles of Association are the widened directors' and officers' liability insurance, the ability for the company to act in the best interests of the parent company, and the ability to do away with the common seal.

Capital Flexibility: Companies will be able to reduce capital without court approval and purchase their own shares (e.g. by buying out a retiring shareholder). This will be useful for example, in closely held companies where a proprietor wishes to retire or transfer his or her holding. The company can simply buy the shares without having to find a purchaser or the other proprietor having to purchase his or her shares.

Easier Administration: Companies will only be required to have one shareholder. They will not be required to have either a company secretary or a common seal.

In some company structures, there is an ability to avoid the requirement for executive directors (i.e. directors that are also employees of the company) to disclose their total remuneration.

Disadvantages of early Re-registration

The disadvantages of early re-registration include;

(a) Major Transaction: The requirement for a special resolution of shareholders who vote against the resolution to pass a "major transaction", and related rights of minority shareholders to require the company to purchase their shares.

(b) Solvency Test: Satisfaction of the statutory "solvency test" prior to the making of a distribution (e.g. a dividend);

(c) Compliance Cost: An increase in compliance costs will occur (e.g. the requirement to prepare an annual report, maintain an interests register, and prepare numerous directors' certificates).

Deemed Re-registration

Any company that has not re-registered prior to 1 July 1997 will be deemed re-registered, and thus automatically be re-registered under the 1993 Act. A number of our clients have suggested that they do not wish to undertake the time and expense of re-registration, but will merely allow their company to be re-registered under the 1993 Act under the "deemed re-registration" regime. We do not recommend this as an appropriate course of action. Deemed re-registration will mean that the existing Articles of Association and Memorandum of Association of the company will automatically no longer apply, and thus all of the particular rights given to shareholders will be lost. Shareholders that are prejudiced by this action will be able to bring an action against the company and, in particular, may be able to force the company to purchase their shares.

Marketing Opportunities

The reforms introduced by the 1993 Act have opened up opportunities for the commercial community. In particular, we believe that valuers that have an understanding of the 1993 Act and the implications it has for directors and senior management of client companies have an opportunity to use that knowledge in the marketing of valuation services, in order to gain a commercial advantage over competitors.

As discussed earlier, the 1993 Act increases the duties and obligations of directors. Coupled with the increase in directors' duties and obligations is an increase in the fines and penalties that can be imposed on directors for breaching their duties, and the requirement for directors to undertake specific procedures prior to undertaking particular actions.

Solvency Test: The first area in which we believe this will open opportunities for valuers is the requirement to satisfy the solvency test. One of the fundamental changes introduced by the 1993 Act is the requirement that directors who vote in favour of making a distribution (e.g. paying a dividend) must sign a certificate stating that, in their opinion, the company will, immediately after the payment of the dividend, satisfy the solvency test, and the grounds for that opinion.

The important points to note here are; It is not the Board as a whole that signs the certificate, but each director who voted in favour of the distribution.

Whether the company satisfies the solvency test must be determined in each director's own opinion, and each director must provide grounds for that opinion. Directors who sign the certificate when reasonable grounds did not exist will be personally liable to the company to repay the company so much of the distribution as is not able to be recovered from shareholders.

Therefore, directors will want to be particularly careful to ensure that, prior to execution of the certificate, their opinion that the company will satisfy the solvency test is founded on reasonable grounds. Moreover, directors will be wanting to create a "paper trail", whereby at a later date he or she can point to certain documentary evidence on which to base the claim that their decision was based on reasonable grounds.

In respect of satisfaction of the solvency test, this "paper trail" will invariably include a certificate from the company accountants or auditors that the company has satisfied the solvency test.

As stated above, one of the limbs of the solvency test is that the assets of the company must exceed the liabilities of the company. However, it may not be enough that the directors merely rely on a certificate from the accountants or auditors if they have certain knowledge that may render assets to be worth less than the liabilities. The requirement for directors to investigate thoroughly is reflected in Section 4(2)(a)(ii) of the 1993 Act whereby the directors must have regard to:

> "all other circumstances that the directors know or ought to know effect, or may effect, the value of the company's assets..."

A common example will be that the fair market value of a property is not reflected in the accounts relied upon by the accountants or auditors preparing the solvency certificate.

Furthermore, the 1993 Act provides that the directors may rely on valuation of assets or estimate of liabilities that are

reasonable in the circumstances.

We are of the view that an opportunity arises here for valuers to ensure that their clients are aware of these provisions - that reliance on a certificate given by the company's accountants may not be enough in many circumstances and that as a result valuations may be required in order to protect the directors voting in favour of the resolution making the dividend or other distribution. In our view, directors will be especially conservative in respect of ensuring the company satisfies the solvency test as the "downside" (in terms of their liability) is so great.

Major Transactions: The second area where we believe there is a marketing opportunity for valuers relates to major transactions.

As discussed, a "major transaction" is the acquisition or disposition of an asset, the value of which exceeds in value the greater part of the assets of the company. All major transactions must be assented to by special resolution of the shareholders of the company.

Companies will want to be satisfied prior to entering into a transaction that the transaction is or is not a major transaction. If it is a major transaction, then the directors will need to factor into the purchase or sale the likely percentage of minority shareholders that will vote against the special resolution approving the major transaction, and as a result may wish to have their shares repurchased by the company. If this is a significant number and the company cannot afford to purchase their shares, the directors may need to reassess whether it is worthwhile proceeding with the transaction. Therefore, it is imperative that the directors make an informed decision as to whether the transaction exceeds in value more than half the total value of the existing assets of the company. In some circumstances, the directors will want to obtain a valuation of the company to ensure that they have accurate figures with which to assess whether the transaction is a major transaction or not.

Interested Transactions: The third area where opportunities arise for valuers relates to transactions in which a director has a personal interest. For example, if a company sells an asset of the company to a non-related company of which a director of the selling company is also a director, that director is deemed to have an "interest". The transaction may therefore be avoided by the selling company if the company does not receive fair value under the contract.

Accordingly, the purchasing entity pursuant to a transaction in which a director has an interest may want to obtain a valuation to ensure that assets they are purchasing are being sold at a fair value. Otherwise the selling company may avoid the contract at a later date.

Compulsory Buyouts: The fourth opportunity for valuers relates to the ability for shareholders to require the company to purchase their shares, for example where the shareholder has voted against a major transaction. Generally, the price of the shares must be fair or reasonable. Therefore, the determination of whether the shares are fairly or reasonably priced may in some situations only be determined by a valuation of assets of the company.

Strategic Alliances: The valuer should be aware that directors who are concerned about asset values will be likely to discuss this in the first instance with their accountants. Accordingly, accounts will in our view be likely to "drive" the decision to obtain a valuation. It may therefore be useful to make a strategic alliance with an accountancy firm to capture the work that will become available in this area.

Summary

Immediate Changes Affecting all Companies

- Directors' duties, powers and liabilities have increased
- Shareholders have greater ability to bring actions against the company
- Directors of subsidiaries are able to act in the best interest of the parent company
- There is a wider ability for directors and officers to be insured and indemnified
- A new name approval procedure has been introduced
- An amalgamations procedure has been introduced
- The law relating to common seals has been relaxed

Reforms Affecting Companies under the 1993 Act only

- The rules relating to capital maintenance have been relaxed allowing share buybacks and financial assistance
- The distinction between public and private companies has been abolished
- Any distribution (including the payment of a dividend) requires satisfaction of a statutory solvency test
- Major transactions require approval by special resolution of the shareholders
- Shareholders who vote against certain resolutions can require the company to purchase their shares
- A constitution replaces existing Articles of Association and Memorandum of Association

Re-registration

- Seek legal advice as to the best time for re-registration for your company
- Advantages of re-registration
  - avoid having to change Articles of Association
  - capital flexibility
  - easier administration
  - ability to waive disclosures of remuneration
- Disadvantages of early re-registration
  - requirement for consent to major transactions
  - requirement to satisfy the solvency test
  - compliance costs
- Avoid deemed re-registration

Marketing Opportunities

- Companies will be required to obtain valuations in respect of
  - solvency test
  - major transactions
  - interested transaction
  - compulsory purchases
- Strategic alliance with accountants is recommended

Further Information

- Should you require further information or assistance in respect of the new Companies Act reforms please contact any of the following at either our Auckland Office Phone - (09- 379-4196) or our Wellington Office - Phone (04- 4727-877);

Wellington	Auckland
David Quigg	Denham Shale
Martin Dalgleish	Matt Pasley
Ross O'Neill	Steve Layburn

(Continued from Page 32)

3.1 Pollution Control Authorities and Courts

Responsibility for day to day environmental management operations, contamination and the escape of wastes to a large extent was originally the duty of local government. The legislative, regulatory and policy bases for all such management emanate from the State Parliament. The main control has now been effectively transferred to State statutory authorities such as, in NSW the Environment Protection Authority (EPA)

The Statutes under which all public authorities function have now mostly been amended to compel the consideration by those bodies of environmental matters even when carrying out or approving activities on Crown land which otherwise required no town planning consent. As a consequence of public pressure, a national environmental protection authority has been established. That body will concern itself with research, environmental reporting, setting and monitoring national environmental quality standards and education.

The Australian and New Zealand Environmental Council (ANZEC) is at present the major environmental body regulating all States, New Zealand and the Federal Minister for the Environment. It publishes draft environmental guidelines.

Environment Protection Authorities are vested with wide powers not only to control the use of land by private enterprise, but also the exercise of functions by all other public authorities if they are likely to affect the environment. An EPA has the power to direct any statutory authority, including local government, to exercise any power which in the opinion of the EPA will contribute to the protection of the environment. For that purpose, the EPA may exercise the powers and function of that other statutory authority at its expense. Owing to the wide definition of "environment", such powers make an EPA potentially the most powerful statutory authority in the State. Thus licences or agreements with local government or a public authority concerning the use of land might be unilaterally altered by direction of the EPA. Local Government or a regulatory authority may be directed to exercise statutory powers to curtail or prohibit the use of land in this way.

Owing to the complexity and technical nature of most new environmental laws, a separate statutory Court known as the Land and Environment Court has been set up in NSW.

It has exclusive jurisdiction to determine appeals and administrative decisions made under environmental law.

It is a superior Court and Judges exercise a supervisory role of judicial review of the environmental laws.

The Court has a wide criminal jurisdiction to hear and determine prosecutions for breaches of environment law.

A most important legislative trend in Australia which affects land value is to give standing to institute proceedings for alleged breaches of environmental laws or to compel compliance with the terms and conditions of approvals, to any person, and not to require the common law test of special injury to the plaintiff. This has resulted in a significant volume of proceedings where a regulatory authority had elected to refrain from taking action.

The value of land has in many instances been significantly affected by private litigation challenging the lawfulness of the use of land or compliance with the terms and conditions of consents, licences and approvals. Such proceedings include the need or adequacy of an environmental impact statement or subsequent compliance therewith.

3.2 Environmental Crime

Most environmental statutes are now divided into "Intentional" offences and into relatively less serious mid-range pollution offences.

Intentional offences enables the more severe penalties to be imposed for "wilful" or "negligent" actions which cause harm or are likely to harm the environment.

Such breaches involve penalties for offences of up to $1 m for corporations, $250,000 for individuals, or seven years gaol. Mid-range offences carry lesser penalties. In most legislation the onus of proof is reversed and directors and managers are deemed personally guilty of offences by corporations, unless brought within limited specified defences. To secure a conviction, the corporation need not be prosecuted. Conviction of such persons is almost inevitable unless at the time of the offence by the corporation an appropriate due diligence programme was in operation.

Whilst such legislation has not displaced the common law presumption that knowledge of wrongfulness of one's acts is an essential element of the intentional offences, it is not always necessary to prove actual knowledge. That the respondent was virtually blind to the consequences . - the act would, in some circumstances, be sufficient.'

In these offences negligence is not difficult to prove, notwithstanding that it is an element of a most serious criminal offence. It is only:

> *"The failure to exercise such care, skill and foresight that would be expected of a reasonable person in the particular situation of the person charged. "h*

What is negligence is a question of fact and may include the failure to take steps to avoid the probable results of intended action.

Experience has shown that it is important to note that negligence includes steps obliged to be taken but not taken under the common law or pursuant to a statute or an instrument issued under a statute. Thus, in appropriate circumstances, failure merely to comply with a licence or its conditions could be sufficient evidence of "negligence" in this context. The consequence is that a mid-range offence may be elevated to a more serious intentional offence merely by failure to comply with permit or licence conditions. In this way a corporation and directors and managers may become liable to conviction of one of the "intentional" offences and exposed to major penalties - including prison for individuals. The financial stability of the corporation unwittingly might in this way be seriously affected by an oversight or inadvertence by employees.

3.3 Strict Liability

The majority of environmental offences created under various pollution statutes are the mid-range offences and are of "strict" liability.'

This means that to secure a conviction guilty intent or knowledge is irrelevant. These offences include the clean waters or clean air offences.

EPA v Ng Court of Criminal Appeal, 13 April 1992, unreported, State Pollution Control Commission v NSW Sugar Milling Cooperative Limited 1991 73 LGRA 86.

Kelly etc Ampol v EPA unreported

Cooper v Australian Oil Refining Pty Limited (1987) 64 LGRA 58.

Even phrases in such offences such as "whether intentionally or not" or "causing or permitting" or "knowingly permitting" in relation to "cause" do not result in such provisions ceasing to be strict liability offences. The word "caused" in strict pollution offences has been held to even include something which occurred, inadvertently, without negligence or without intention.'

Consequently it is not difficult to obtain successful convictions for pollution of a watercourse even when arising out of a breakdown of a system on adjoining land which was apparently appropriate when installed.

The ease of which conviction for these offences can be obtained was highlighted by a judge who observed that the wide statutory definition of "pollution" and "waters" could include the act of putting chlorine in backyard swimming pools or lfuoride in water supplies.9

In respect to similar offences, Victorian courts have said there is no defence and NSW courts have said that the only available defence is "honest and reasonable mistake". This means that the defendant may raise a reasonable doubt that there was a belief in a mistaken set of facts which, if true, would render the act or omission innocent.

However, when raised, most attempts to establish the defence have been unsuccessful. In a prosecution for breach of licence conditions it was accepted that the defendant held an honest belief that the licence conditions had been set as "targets", not maximum levels. Breaches had frequently occurred with the knowledge of the prosecutor and such conduct had never led to prosecution. However, such belief was nevertheless held to be unreasonable. In another case10, as a result of a break in an underground pipeline, oil escaped from the defendant's property into a creek. The depot manager never saw cause to question the integrity of the pipe nor ever perceived the possibility of its failure. The defence again failed.

Even the taking of all due diligence is not available in some States either as a separate defence or as part of the honest and reasonable mistake defence to a strict liability offence." This may come as a surprise to many corporations who believe the existence of appropriate due diligence programmes is a defence to any environmental offence.

Most environmental crime is committed by corporations and their exposure to prosecution has been highlighted by calls for privilege against self incrimination. The vexed question as to common law privilege against self incrimination by corporations his been comprehensively reviewed and explained recently by the High Court of Authority." A corporation is to be distinguished from individuals, and the privilege does not apply. A statute may deny that privilege. Notice to provide information may even be given under a statute after the commencement of proceedings and even if the notice was given for the sole purpose of gathering evidence for a prosecution.

This decision exposes potential problems for directors and persons concerned in management of a corporation. Whilst such individuals have the right to maintain silence, the corporation might be required to produce information which might reveal a breach by the corporation. Such persons are deemed automatically guilty of offences committed by a corporation unless one of the prescribed defences can be established. The corporation which produced the information need not be prosecuted for a director or person concerned in the management to be prosecuted.

This might in some situations be a matter of real concern. A person concerned in management of a corporation is not defined and is a question of fact in each case. Lenders, asset managers, real estate managers, rent collectors and the like, may in appropriate circumstances be deemed guilty of corporate environmental offences.

3.4 Vicarious Liability

Notwithstanding strict liability and potentially severe penalties, contravention of a mid-range offence has been held to operate to make a master who had no guilty intent or even knowledge of the breach, vicariously responsible for the conduct of an employee. It is not even a defence that the employee had no authority and would never have been given authority to commit the particular act. Conduct which was a mode, although even an improper mode, of performing a function that a person was employed and authorised to carry out is within that responsibility. Vicarious responsibility also probably extends even to similar actions of employees of independent contractors. This remains to be judicially clarified.

The Court has convicted a company for polluting waters, even though the acts causing the pollution were carried out by an employee of a contractor.

In that case, the company was undertaking repair and maintenance of a fuel system at its power station and engaged a contractor to undertake part of this work. A number of pipes containing oil and tar were to be removed. To prevent pollution, the pipes had to be cleaned before they were cut. They were cut without being cleaned, which resulted in a large quantity of oil escaping into a drain and eventually into a creek. Neither the corporation's supervisor nor the senior company engineer was present when the pollution occurred. The submission that the employee acted beyond the scope of the contractor's agency failed.

In another case an employee had the responsibility to monitor the level of a leachate dam which collected polluted water. Without authority and without knowledge of his employer he deliberately breached the dam wall and allowed the escape of polluted water.

The employer was convicted of the offence of polluting a nearby stream. The court held that the employee was still carrying out his duties even though in an improper manner.

Not only in those circumstances was the corporation guilty but the directors and managers were deemed guilty as a consequence of the improper acts of the employee.

3.5 Polluted Sites

In Australia, the assignment of liability for the cost of clean-up of soil pollution of sites is fast becoming one of the most significant issues facing industry. Land

Tiger Nominees Pty Limited v State Pollution Control Commission Court of Criminal Appeal (1992) 75 LGRA 71.

9 SPCC v The Electricity Commission of NSW, Bannon J, 11 October 1992, unreported

'0 State Rail Authority of New south Wales v Hunter Water Board, NSW Court of Criminal Appeal. 24 November 1992.

Australian Iron & Steel Limited v EPA[19921 79 LGRA 158

12 *EPA v Caltex Refining Co Pty Limited* [1994] 68 ALJR 127

use can be seriously affected because a control order can, notwithstanding the otherwise lawfulness of the use either;

- absolutely prohibit specified activities in relation to a declared waste;
- prohibit them unless they comply with specified conditions;
- prohibit them unless they are individually licensed and comply with licence conditions; 13
- order clean-up to be carried out at occupier's expense; or
- prevent polluted discharge from the premises.

Most industries, particularly if long established, produce some "waste" which pollutes the site. Changing standards can make previously acceptable land fill (e.g. furnace ash) an unlawful contaminant.

Liability for clean-up is now an important issue in the sale or lease of all land (particularly industrial land) or the acquisition of a business. Clean-up costs in many cases far exceed the market value of the site itself. Liability for clean-up is most commonly imposed upon the occupier but also on the actual polluter, owner and in some situations former owners.

4. The Lawfulness of the Use of Land

The development of land in all States for most purposes is regulated by a town planning act. Any new development or modification or intensification of an existing development usually requires the consent of the responsible authority, usually the local Council. Until relatively recent years the possession of a development consent was a guarantee for the lawful continuation of the use of land. This is no longer necessarily the case.

Almost every sphere of Government in Australia now has an involvement in the control of the environment e.g. in NSW there are 80 statutes regulating environmental issues in the chemical industry. In addition to obtaining development approval, there is an increasing need to obtain approvals, or licences, from various government authorities e.g a licence to discharge pollutants will be required from Regulatory authorities which are endeavouring to get uniform standards in each State for discharge into the environment. The absence of a licence or failure to comply with conditions is an environment offence. Approvals may require the development to be carried out in strict conformity with the provisions of an Environmental Impact Statement. Licences or permits may also be required to import or export hazardous waste,14 to store dangerous goods," or deal with hazardous chemicals."It may be necessary to enter into agreements with the Water Board to take trade effluent produced by the premises.

Compliance with such conditions of licences and permits is assuming increasing importance under environmental laws. Failure to comply with such conditions can not only be evidence of lack of "due diligence" but also as previously discussed, elevate an offence to a more serious level of negligence which imposes more significant penalties. Such breaches, and the industrial activity on the land may be restrained by injunction from the Courts. What is not generally known is that failure to comply with conditions of a consent, approval or licence in some cases may even render the permit void.
The existence of a valid development consent, necessary licences, permits and compliance with conditions attached thereto are critical factors to determine liability under pollution control statutes. Past compliance with conditions of a lice,ice or a development approval and the real likelihood of ability to comply in the future are often overlooked in the determination of the value of land or the business thereon.

There has been a growing tendency of conservation groups to challenge the lawfulness of approvals on environmental grounds. There is now a trend in environmental legislation to copy town planning statutes which vest a right to institute proceedings to restrain a breach to "any person"." Such easier access to the Court has resulted in a steadily increasing number of proceedings to challenge the validity or to compel compliance with conditions of a development consent.
Some States have bowed to strong public pressure to even give similar standing to third parties to institute criminal proceedings under pollution law to prosecute where the EPA has elected not to take proceedings. This is a significant shift in enforcement policy, particularly because of its effect in situations where the EPA would not prosecute because it was implementing a long range policy to gradually upgrade pollution discharge levels for long established premises.

Major legal challenges have also been instituted by trade competitors merely to frustrate or restrict opposition activities. Proceedings have instituted to question, on environmental grounds, the lawfulness of consents or to enforce compliance with conditions, e.g Woolworths, in a number of States, sought declarations as to the validity of permits issued to a trade competitor to operate a cash and carry grocery business from a warehouse. The approval was said to be prohibited by the environmental planning instrument.

In another case a waste recycler sought declarations and injunctions to restrain the continued operation of a competitor by challenging "existing use" rights to operate without a permit under the planning instrument.

However, the most common threat to industry is community group challenge or pressure on local authorities to institute proceedings. Many industrial and commercial operations which previously had been carried out for many years have had permits declared void, existing use rights revised and conditions of consent enforced by injunction.

The possibility of private or regulatory authority litigation to enforce conditions imposed upon approvals or licences must compel a close examination as to the appropriateness of such conditions and continued ability to comply therewith if such licence is essential to future land use. It is now obvious to industry that unreasonable or unachievable pollution levels in conditions must be altered if the continued operations of the activity not be put at risk.

[3] e.g Environmentally Hazardous Chemicals Act, 1985 (EHC Act).
[14] Hazardous Waste (Import and Export) Act, 1989 (Cth).
[5] Dangerous Goods Act 1975
[6] Environmentally Hazardous Chemicals Act, 1985.
[7] EPA Act] 979,s.123.

5. Some Trends

From the above it is seen that most Australian environmental legislation has traditionally only been two dimensional ie. a perceived need to:

- meet domestic environmental concerns and community expectations; and
- fulfil obligations imposed by international conventions.

As noted, the inevitable result in many cases however was merely to punish for environmental offences and ignore the adverse impact upon industrial competitiveness and its trading positions.

Fortunately, some recognition of the need for a sound economy to achieve a sound environment was highlighted by the National Strategy for Environmentally Sustainable Development in 1992. This was some recognition of the high administrative costs of a "command and control" regime to merely punish "end of pipe" pollution control. It was recognised that such systems are slow and generally should be regarded as only effective as a partial tool to control and protect the environment. It is now recognised that any environmental control strategy must be backed with a tough penal system, but greater benefit will be achieved by compelling or encouraging private sector monitor and control.

5.1 Economic Incentives to Control Discharges"

A number of economic incentives have been tested e.g:

(i) Performance bonds

In Australia, performance bonds are negotiated between the government and industry, as there is no general legislative authority.

Discharge performance bonds usually take the form of a predetermined sum to be forfeited to the control authority if a certain action is not undertaken by a company within a designated time and to a certain standard. There are, in effect, predetermined civil penalties for failure to comply with environmental requirements. They act as an incentive for the polluter to comply with pollution controls because if they do not, the result of forfeiture of the penalty would be greater than the cost of the controls. If the bond is equivalent to the amount of expenditure required to implement controls, then there is a definite incentive for the company to implement those controls.

(ii) Tradeable Pollution Rights

In Australia, owing to a perceived failure of statutory control, one of the recent. pushes to effect pollution control has been to rely upon market forces rather than government regulations. It has been argued that a system of tradeable pollution rights should be established. They have been defined as:

> *"Quotas, allowances or ceilings on pollution emission levels of specified polluters that, once allocated by the appropriate authority can be traded subject to a ..... of prescribed rules."*

The basic principle is that if a company which has been allocated a certain quota of allowable pollution is able to reduce its pollution below that quota, it may sell the unused quota to other parties. The value of these "rights to pollute" would be determined by market forces.

Again, we may follow the trend in America, where the Chicago Board of Trade has voted to create a marketplace where utilities and speculators could buy and sell those rights to pollute. America's Clean Air Act allows utilities to accumulate credits for keeping emissions within limits and to sell excess credits.

(iii) Pollution and waste disposal charges

Consideration is being given to the advantages of pollutant emission charges and waste disposal charges which could directly encourage industry to reduce the quantity of pollutant emitted or waste generated by a site. They are generally calculated on both the quantity and type of pollutant or waste discharge. The imposition of charges is generally directed at raising revenue to cover regulatory costs, research or restoration relating to the environment.20

(iv) Levies

The essence of an environment levy is that it is generally applied on a specific product or activity to meet a specific environmental purpose. The levy is usually imposed upon the activity or product which gives rise to the environmental problem to which the monies are to be applied. The levy does not usually take into effect the level to which each person levied contributes to the environmental problem, ie., it tends to be "across the board".

The advantage of levies is that they are relatively simple to impose and collect and they can raise specific amounts of money relatively quickly and simply in order to combat specific environmental problems. They do not, however, act as incentives for industry to reduce its waste production as they do not take into account actual levels of waste or pollution emitted.

The notable example of the imposition of levies is the United States Superfund Levy. Because of the difficulty in identifying all the responsible parties for causing contamination to land, and because enormous amounts of money are needed to be raised relatively quickly to enable the American authorities to implement clean-up procedures, the Superfund Levy was imposed at varying rates on various industries, depending upon the nature of the industry."

5.2 Compulsory Waste Minimisation and Recycling

Recycling in Australia is primarily managed by the private sector, although governments at all levels have some influence. Local governments influence recycling indirectly through their waste disposal policies and directly through the manner in which they collect waste. State governments influence recycling by exercising control over local governments, through their legislation and policies relating to environmental and industry development and by their own purchasing policies. For example, South Australia has legislation applying to specified beverage containers and the Victorian State Government has negotiated recycling targets with industry.

To date, Australian governments have declined from using across the board

[1"] Economic incentives have been examined by the Australian Industry Commission in its Report on Recycling, Australian Government Publishing Service, 22 February 1991.

['9] OECD

[20] Court J, Using Government Mechanisms for Minimising Environmental Damage, paper delivered to IIR Pty Limited Conference (Environmental Damage), 20 May 1991, Sydney.

[21] see Moore J, et al (1989), Using Incentives for Environmental Protection, and Overview, CSR Report for Congress (Washington).

recycling legislative standards which may be insensitive to the industry involved. However, many people in Australia think that industry should he forced into recycling all of its waste. It is uncertain whether the governments in Australia will legislate to require waste minimisation and recycling or whether they will merely encourage this by legislating for economic incentives such a those discussed in s 5.1. It may be that governments will merely adopt measures by way of policy and education rather than regulation.

The Industry Commission Report[22] recommended that Australian governments need to review legislation and regulations which are necessarily disadvantageous to recycled materials or favours one form or level of recycling at the expense of another. It also recommended that governments need to ensure that when promoting recycling they accord with the principles of public administration.[23]

Private Sector Monitoring

A. Accredited Licensing/Private Sector Monitoring

Owing to the lack of resources and the enormous administrative costs in policing licences, some States (particularly Victoria) propose to implement an "accredited licensing" system for an industry which will, or is likely to pollute.

Approved premises will be issued a license which will grant a high degree of operational freedom and an obligation to obtain approval only for major works. Conditions precedent to obtain such accreditation are the existence of a satisfactory:

(i) environmental management system

(ii) environmental audit programme; and

(iii) environmental improvement plan.

However, the Chief Executive Officer of the licensee corporation will be required to personally certify compliance with all licence obligations in a performance report. Whilst this system has some obvious advantages, certification and reporting might provide regulatory authorities with the means to prosecute or expose the corporation to liability for clean-up or rehabilitation costs.

B Due Diligence Programmes

Evidence of the exercise by a corporation of due diligence to prevent the commission of an environmental offence is essential to establish a statutory defence in most environmental crimes.

As previously noted the only real defence available to directors and managers is "due diligence" to prevent the contravention. General "good housekeeping" or due diligence is not sufficient.

Many corporations have implemented appropriate environmental programmes. These programmes must include an adequate environmental audit and ongoing monitoring and reporting regime. The absence of a programme makes conviction of directors and managers of strict liability offences almost inevitable.

Whilst such programmes have probably been instituted to protect the corporation or director or manager from prosecution, the obvious benefit to the community is that the environment is thereby protected also.

A survey of industry generally revealed that:

- 45% of corporations had established a formal environmental management system;
- 85% were generally aware of environmental obligations;
- 40% saw the environment as a threat; but
- 73% saw the environment as a business opportunity.

The implementation of a due diligence programme is even more important where the corporation carries out its operations pursuant to a licence or permit which is subject to conditions. As previously discussed the directors or manager must ensure compliance with such conditions to avoid being exposed to the more serious environmental offences which carry prison and severe penalties or expose the licence itself to legal challenges.

C Warranties and Indemnities

Most corporations and asset managers are now more conscious of the constantly changing environmental obligations imposed by regulatory authorities on owners and occupiers of land, retrospective liability for clean-up and changing pollution standards. Most major industrial land or business acquisitions now involve some assessment of environmental matters.

Prudent vendors or purchasers commission environmental audits of the land to:

(a) exercise some control over the quality and scale of an environmental audit;

(b) identify the actual condition of the premises at date of sale; and

(c) accurately estimate possible clean-up costs and which might affect value of the land or the business.

Obviously some vendors are reluctant to commission a report which, if it gets into the wrong hands, might affect the sale price of the land or even make it unsaleable. There have been cases where the sale aborted but the audit exposed the owner to prosecution and clean-up orders. On the other hand, if the nature and extent of pollution is likely to be an issue in the sale the vendor is likely to be in a better position if it had control of the preparation of the report. It would be imprudent for a vendor to give indemnities and warranties concerning contamination in the absence of an audit report.

D Covenants

Leases of land usually include well known covenants to keep the premises in good repair and deliver up the premises at the end of the term in good order and condition, wear and tear excluded. Most conveyancing statutes deal with similar matters.

However, most people assume that notwithstanding such covenants that a lessee can never be obliged to repair damage which had been caused by a previous tenant or to return the premises at the conclusion of the term of the lease in better condition than at its commencement (excepting wear and tear).

These and other similar issues are now the subject of major litigation in Australia concerning a very large site, used for many generations for industrial purposes. The site was reclaimed over decades prior to the subject lease. The filling on the land contained vast amounts of ash and other industrial waste generated by previous

[22] Industry Commission Report: Recycling in Australia, Volume 1, Report No.6, 22 January 1991.

[23] Volume 1, p.15.

occupiers. The land was leased for industrial purposes to a corporation whose main or only client was the lessor.
The lessor has made a claim for huge sums for rehabilitation of the land on the basis that the said covenants imposed upon the lessee obligations:

(i) to repair the filled site by the remediation or removal of contaminants placed therein by previous occupiers;

(ii) to repair the site by the removal or remediation of poorly compacted fill placed by previous tenants;

(iii) to hand back the premises in a condition which does not include any contaminants, i.e;

- remediate the site to ANZEC residential standards even though leased for industrial purposes.

There is some public awareness of the issues raised in this matter. Prudent lawyers are now advising lessees of industrial or other likely polluted land to demand or commission an environmental audit prior to any agreement to lease.
Lessors are increasingly being obliged to indemnify the lessee against possible clean-up costs and obligations under environmental laws arising out of the condition of the premises at the commencement of the lease. Many business acquisitions have aborted on this issue.

It is not generally known that no enforceable indemnity or warranty can protect the lessee against future prosecution for environmental offences. Similarly, nor can a person obtain insurance against the possible liability to prosecution for an environmental crime.

An occupier (lessee) of premises which contains contaminated ground water which is discharged from the premises through no fault of the occupier is still strictly liable for such pollution. A major corporation was prosecuted in similar circumstances for a polluted discharge even though it could prove that such pollution could not have emanated from any activity on the land by the occupier. The pollution apparently emanated either from adjoining premises or contamination from the site itself. The occupier was convicted of pollution.
The first above-mentioned dispute between lessor and lessee is almost certain to proceed to the High Court on these important questions of law. If the lessor is ultimately held to be correct it places lessees in an invidious position. Whilst the situation is probably more serious for leases of industrial premises the problem obviously extends to the rural, commercial and even residential leases. Most rural land and dwelling sites contain pesticides, nutrients or other chemicals consistent with past usage. Many sites in older residential areas are likely to contain heavy metals such as lead at unacceptable levels arising from paint scrapings and exhaust fumes from vehicles.

E Rezoning and Development Applications

The quality of land is obviously most relevant not only to its value but the manner in which it should be used or developed. The trend is now to require an environmental audit prior to the consideration of any application for rezoning or proposed major development approval. It is most likely that this trend will be made mandatory in all cases by appropriate legislation.

Obviously, the value of undeveloped land or land with rezoning potential can be seriously depreciated by existing contamination. The need to remove pesticides and other chemicals from farmland revealed in audits has in a number of cases made rezoning for residential purposes non-feasible. As previously noted the existence of an environmental audit which reveals contamination might expose a wide range of persons to clean-up costs and even prosecution. Such obligations might be incurred even if the rezoning or development application is refused.

F Lending Institutions

Financiers are now acutely aware of environmental issues which might affect the value of a security viz:

(a) the impact of environmental requirements on the borrower's financial performance (cash flow);

(b) the impact on the value of security; and

(c) liability of the lender if it exercises "management and control".

G Financial Performance

Financial performance of the borrower (i.e cash flow) can be affected by:

(a) conviction of a pollution *offence;*

(b) costs and damages of clean-up from a pollution offence;

(c) statutory and court orders to install pollution control equipment;

(d) the liability to clean up contaminated land and ability to comply with conditions of licences and permits.

A significant factor now taken into account by lenders in assessing the environmental risks of an activity is the appreciation of and response to those risks, by the borrower.

Lenders now insist on the existence of a practical, effective environmental management programme to reduce the likelihood of a serious pollution incident.

The value of security

The lender will require that environmental risks associated with ongoing and/or past activities be assessed in respect of:

(a) the impact on the value of security; and

(b) the lender's liability on realisation of the security.

The greater the environmental risk the greater the likelihood of an adverse effect upon the value of their security.
Financiers are now entitled to expect a valuation of land to properly assess all relevant environmental factors. Failure to do so, even without express instructions might be evidence of negligence. A valuation may be required in many cases to consider:

(a) likely or actual site contamination;

(b) consequential restrictions in redevelopment potential;

(c) impact on the premise's income potential; and

(d) distortions in comparable sales analysis.

The Australian Institute of Valuers and Land Economists has recognised the problem and produced a practice Standard on the Valuation of Contaminated Land. It provides a list of environmental risk activities. The Standard emphasises the need for further investigation and audit by an environmental expert once a potential problem has been identified.

One cannot over-emphasise that valuers should not hold themselves out to be experts in the area of environmental risk assessment and that appropriate independent experts should be contracted where appropriate. In any event extreme care must be taken to make it abundantly clear in any valuation that it does not advise on environmental matters but is based solely upon the independent expert advice.
In Australia, there is uncertainty as to when a lender may be exposed to liability for environmental risks if it assumes a position of management and control in order to protect the security. Whilst liability is likely to occur in a formal administration, as owner and/or occupier, it may also indirectly occur through informal management, corporate advisory

roles or monitoring pursuant to a Loan Agreement. It is a question of fact and degree in each case.

Both Victorian and New South Wales environmental legislation impose personal liability not only on each director but also on the "person concerned in the management" of a corporation.

It is possible that under environmental legislation the lender or its agents may be construed as "persons concerned in management of the corporation" or in control of premises, that is, as an "occupier" under the definitions in the environmental legislation.

In the USA[24], a secured creditor was held liable under CERCLA without being actively an operator. The creditor was held liable merely by participating in the financial management of a facility to a degree indicating a capacity to influence the corporation's treatment of hazardous waste.

A financier must be in a position to ascertain whether they and/or their agent are or would be in a position of occupier or "management or control", if to elect whether to accept the environmental risks.

5.3 Legal, Professional Privileges and Environmental Audits / Valuation Reports

Environmental audits prepared for due diligence programmes or for financiers or other land valuation purpose might be used by regulatory authorities for prosecution or clean-up orders. For this reason legal professional privilege against production of such documents is often sought. However, whilst most regulatory authorities have stated that voluntary environmental audits and similar reports will not be procured or relied upon by the prosecution unless raised in a due diligence defence, concern has been expressed as to reliance upon such statements.

Much confusion appears to exist as to the ability to obtain legal professional privilege in respect to the production of reports even when prepared for or at the request of legal advisers. This is a complex topic which will not be fully discussed here but - some points can be briefly made:

(i) environmental audits initially procured for valuation or due diligence or other administrative purposes even if later submitted for legal advice will not necessarily be protected.[25]

(ii) Even if such documents are procured at the request of the legal adviser they will not necessarily be protected [26]

(iii) Documents obtained from investigators or experts retained by legal advisers on the explicit instructions of a client will be subject to legal professional privilege if:

(a) they were created solely for the purpose of submission to legal advisers for advice or for use in litigation; or

(b) were procured when litigation is threatened or contemplated [27]

The most prudent course where legal professional privilege is essential is not to prepare a report unless and until it is expressly commissioned by the client for the purpose of legal advice or litigation.

6 Conclusions

(i) The protection of the environment and the remediation of contaminated land are now firmly established as issues of public importance, and legislative control and government policies will inevitably continue to significantly affect industry and commerce.

(ii) That public concern has resulted in the rapid expansion of legislation creating significant environmental crime and clean-up liability.

(iii) Development of all land, including Crown land, is now subject to sensitive environmental assessment prior to the granting of approval of rezoning or development applications.

(iv) However, the traditional principles of criminal law are not wholly appropriate' for environmental crime.

(v) Regulatory authorities in Australia have in the past demonstrated a preference for:

i) criminal prosecutions rather than civil enforcement of environmental laws;

ii) prosecution of individual as well as or in lieu of the corporations which employ them;

iii) increasing the liability and range of persons responsible to clean up polluted sites.

(vi) However, the trend now is to encourage measures to prevent or remove environmental harm rather than merely punish after the event.

(vii) Whilst civil enforcement will reduce some criminal actions, industry must accept the inevitability of the imposition of economic incentives and threats to control pollution.

(viii)- The private sector will increasingly monitor and control the environment by the distribution and imposition of obligations to assess and accept obligations to mitigate pollution.

(ix) Private sector audits and monitoring programmes may increase exposure to prosecution and clean-up costs and significantly affect the value of land or business. Legal professional privilege should be acquired in appropriate circumstances.

(x) The valuation of land must increasingly take into account the likelihood and financial impact of site contamination and environmental risk.

(xi) Valuers should be vigilant not to assume or appear to assume expertise or responsibility for the assessment of environmental risks.

24 *United States v Fleet Factors Corporation* [821 F Supp 707 (1993)]

25 *Grant v Downs* (1976) 135 CLR 674. A 1992 Canadian decision *(Ontario [Ministry of the Environment] v Tetrault)* confirmed that documents created for legal advice can be subject to legal professional privilege although the prosecution sought to establish that the documents were part of an audit created for management purposes rather than for legal advice.

26 *Morlea Professional Services Pty Ltd v South British Insurance Co Ltd 27* September 1984, unreported, Foster J, Federal Court.

27 *Wheeler v Le Marchant* (1881) 12 ChD 675, *Nickmar Pty Limited v Preservatrice Skandia Insurance Ltd* 1985 3 NSWLR 44.

TEOHOOIOSY fORUM

Compiled by Ian Mitchell

One of my objectives as compiler of Technology Forum is to provide articles that cover the interests of a broad range of users. In this Issue of the Journal, the first* article discusses the differences and applications of various types of databases and the second article covers some up-and-coming changes to VNZ-Link.

The opportunity exists, if you have a particular skill or knowledge in a technology related field or know of someone who has, to submit articles for publication in Technology Forum. It is it good way to share your specialist knowledge and to perhaps raise your profile within the property industry. I would be interested in hearing from you or to receive any articles you may wish to submit for publication in Technology Forum. I can be contacted at Darroch & Co PO box 27 133, Wellington on (04) 384 5747, or through the Head Office of the New Zealand Institute of Valuers.

Where Do You Put That Data? Options Explained

by M Bain

Martyn Bain is *a valuer in the Wellington Office of Darroch & Co Ltd. Ile* is *responsible for the day to day management of the Wellington computer system. Martyn graduated from Lincoln University in 1990 and has since worked with Darroch & Co Ltd, principally in their Commercial and Industrial division.*

Most valuation practices now use computers in one form or another. Word processing programmes and Valpak are now commonplace. A number of offices also have a full professional "suite" of programmes. A typical suite includes word processing, spreadsheets and database programmes all packaged together.

Most modern programmes allow for data entry, storage and manipulation in one form or another. It is critical in today's environment to choose the correct programme or application for the task.

Computer users today generally know how to operate the programmes they use most frequently, but often don't understand the function of others. Specifically, manual filing systems have historically dealt with data related problems.

The aim of this paper is to firstly explain the three common types of computer programmes that store data, and secondly, detail in straightforward terms the workings of a database.

The Three Options

Word processing programmes provide powerful "text" manipulation facilities, but are not designed to manipulate mathematical (tabular) data. A word processing programme enables storage and retrieval of data in text (character) format. There are no user-friendly features that will select files by value unless a defined set of retrieval criteria is used for accessing data "embedded" in word processing files or file names. For example, you cannot ask the programme to select all valuation reports that have a value greater than $150,000 and less than $200,000 unless a predetermined "address" is incorporated in the file. A word processing programme is similar to a manual filing system, however with distinct administrative and presentation advantages in the hands of a competent operator. Required files can be easily accessed once identified, modified if need be, and stored in a compact form.

Spreadsheet data manipulation relies upon accessing and influencing a strict discipline of "tabular" math-based addresses (cells). Most spreadsheet programmes now feature comprehensive database facilities. Spreadsheet database facilities do have certain limitations. The maximum file length (assuming you have the fastest and largest personal computer available) is around 16,000 records. The standard personal computer would struggle with a database of that size and any manipulative tasks would be slow. Spreadsheets are not designed specifically for database work. The most appropriate use of a spreadsheet is for "notepad" or "what-if" type calculations. Thus, the spreadsheet is ideal in

situations where a set of independent variables need to be placed into a calculation. If the calculation were done by hand, the changing of any value at the top of the calculation would require its complete rework. A spreadsheet will automatically update your calculation provided appropriate formulas are used.

Databases are quite different to word processing and spreadsheet programmes. A multitude of information can be stored on a database. It is important that this information is stored in the appropriate format for future use. As with word processing software and spreadsheets, a well-designed database will provide easy access to stored information or data.

Databases

Originally, database programmes existed in single or "flat-file" format only advanced programmers were able to operate. Flat-file programmes became increasingly user-oriented, advancing to a point where most new database programmes and spreadsheets are now "user-friendly" and fully featured.

Database programmes continue to develop in leaps and bounds and the most complicated multi-file database functions have become streamlined and "quick".

A flat-file is a single file; each record is independent. The Valpak Sales database is an example of a simple flat-file database. Each sale is a "record" and occupies one "row" of the database. Duplication of address, valuation reference, legal description and sometimes Government Valuation information will occur if a property sells more than once. However, properties do not tend to be resold quickly so this duplication does not create large amounts of unnecessary data within the Valpak database. It may however cause problems in other applications.

A relational database programme can use either a single database file or a collection of database files, linked together by unique identifiers. Data duplication commonly occurs in the flat-file database, whereas a relational database significantly reduces duplication.

It may be difficult to understand why this data duplication can become a problem. Consider the case of a mailing-list database where the address of a company changes and there are 20 different contact people from that company on your database.

(see diagram)

In "A" the flat-file database, you have to individually go into each of the company's employee records and change the address. The relational database "B" however, requires only one change. The operation is less time consuming and there is less chance of error.

There are many relational database programmes currently available on the market. Microsoft Access is an example of a user-friendly database, and of course, there are others. Microsoft Access uses four simple "modules" each providing an ideal heading with which to demonstrate the workings of a database. Other programmes use similar modules, sometimes under different names.

Database or Table

A database is a list of information or records. Each record can have any number of "fields" (for example, name, address, city etc). Fields can be one of three basic data types:

Numeric/Data	Numbers Only
Character	Includes any combination of numbers and characters limited to a length including all characters and spaces of around 255 characters.
Memo	For large strings of text, i.e greater than 255 characters.

There is a difference between numeric and character fields. With numeric fields you can perform mathematical operations with ease including sorting and ordering. Using a character field, these tasks become a little more difficult. For example assume you had a field "street number" with the following numbers - 1, 3, 1 1 , 21. If the field is designated as a character field and the data is sorted in ascending order, then the order would be 1, 11, 21, 3 (i.e sorted by first character, then second character and so on). If designated as a numeric field the data would be ordered in conventional numeric order.

While spreadsheets are limited in the number of records allowed, available "memory" and the capacity of the PCs "hard disk drive" are the only limits to database file size.

In addition, the database file can have an "index" file associated with it. The index file is an advanced database feature. In a database programme, the physical order of the data in a file remains exactly the same (that is, the first record entered is at the top of the file and the last at the bottom). An index file "masks" a database file so that it appears in order. The index file works much faster than spreadsheet sorting, and in addition speeds up data searches. Instead of looking through every record to find a "match" a database programme makes use of the index file to start a search closer to the target.

Form or Screen

The display of Spreadsheets, and indeed database tables (as shown), are in "row/column" format. A database form or screen is an automatically designed, or user-defined input or manipulation "template" which can be designed to "mirror" existing manual input forms. This enables faster entry, with a logical, familiar layout allowing information to be entered or edited more easily on the screen. Forms also allow for the entry of information in one, two, or three linked database tables at one time.

Query

The database/table and form/screen options are utilised for the setup and entry of data in a database. A "query" manipulates and extracts this data.

Data Manipulation

Data is manipulated using queries. A query can add calculated fields to a database. A calculated field is similar to an additional column in a spreadsheet. A full range of calculations is usually available. A user could simply add numbers from two separate fields or perhaps compute a more detailed calculation. For example, to calculate a depreciation factor, a range of fields including square metre area; replacement cost rate per square metre; age and depreciation rate per annum would need to be used.

Data Extraction

Data can be extracted from databases using defined criteria. For example: equal to a "Market Valuation" greater than $150,000, less than $200,000 and ordered by address.

Once a manipulation and extract framework is defined a query is "run". A query can then be held in the computer memory (that is lost when you "exit" the application, unless saved to file), and printed if desired.

A query demonstrates the difference in power between a database and a spreadsheet. In the past, queries have tended to be the business of trained computer programmers. In spreadsheets, you usually save a selection or extract in a secondary version. This requires more disk (storage) space. In a database you save a query, that is, the instructions to extract the information. In most modem programmes these instructions are called SQL (Structured Query Language). SQL mimics standard English and is easy to learn.

The benefit of a query is twofold. First it saves disk space, but more importantly tidies up where there are changes in data. To update a spreadsheet you will want both version one and version two of the data to stay the same. In a database, there is only ever one version. A change in the main database table will register in all future or subsequent query updates - the equivalent of spreadsheet "versions".

Queries can also cross-tabulate data. Cross-tabulation queries are somewhat difficult to follow. A cross-tabulation summarises data. Assume within your Mailing List Database, you have additional fields - Business Type (Bank, Accounting, Lawyer and so on), and Region (Wellington, Auckland and so on). You could design a cross-tabulation query that summarises your mailing list by showing the number of Companies by Business Type and Region (see diagram).

Report

A report either prints the data or displays it on screen. A report can show the "raw" data (original table data) or alternatively it can display the results of a query. Data can also be grouped within a report.

Grouping eliminates repetitive printing of headings and so on. Data can be sorted - to order your data A-Z, 1-9 - and numeric fields can be totalled and subtotalled or statistically analysed within a report. The count function is available for character fields.

A report is like a query when saved. When saving a report you are actually saving the instructions, not the formatted data itself (as you would if using a spreadsheet). These database functions conserve hard disk space. More importantly, changes in main data files are carried through to final reports.

In addition to the aforementioned "modules" are "programme", or "macro" modules that can automate and customise your database. Most modern database programmes have much of this automation "built-in", converting time-consuming or complicated tasks into user-friendly tasks.

Programs and macros, while increasingly easy to learn, are quite a separate topic outside the scope of this paper.

Summary

In summary, the key features of databases and spreadsheet programmes are:

Databases

- Can handle large amounts of data (unlimited length).
- No duplicate "versions" created.
- Simplified data input and customised data output.

Spreadsheets

- Designed for complex calculations (financial, cash flows etc).
- Ideal for smaller data groups that require intense manipulation ("what-if' analysis etc).

Modern computers are powerful tools if used well. Each programme has its merits and drawbacks. A computing task can be approached from a variety of angles. There is no right or wrong way, any new task must be carefully planned. Initial objectives must be clearly defined with information available. Limitations and needs must be identified and output requirements determined. The user must then be careful to select the correct programme or application for the task at hand.

Mailing List "A"

Company Name	Address	Town	Name
Brown & Co	56 River Road	Christchurch	R Brown
Brown & Co	56 River Road	Christchurch	M Black
Brown & Co	56 River Road	Christchurch	P White
Brown & Co	56 River Road	Christchurch	T Taylor
Smith & Co	123 Main Street	Wellington	R Smith
Jones & Co	34 High Street	Auckland	B Jones

Mailing List"B"

Company Name	Address	Town	Company
Brown & Co	56 River Road	Christchurch	1
Smith & Co	123 Main Street	Wellington	2
Jones & Co	34 High Street	Auckland	3

Z
linked

Company	I	Name
		R Brown
		M Black
		P White
		T Taylor
		R Smith
		B Jones

1

VNZ-Link Developments

by K J Cooper

Kelvin Cooper is Deputy Valuer General and is primarily responsible for the marketing and finance functions of Valuation New Zealand from the Wellington head office.

He is a Fellow of the NZ Institute of Valuers and is a chartered accountant, and a member of the New Zealand Computer Society. Kelvin Cooper holds a Master of Public Policy degree and a Diploma of Public Administration from Victoria University. He has held senior positions in Housing Corporation, Department of Lands and Survey and Tourist and Publicity Department.

The VNZ-Link service provided by Valuation New Zealand is now 5 years old. Its introduction in 1989 replaced the previous Videotext PROVIDES property enquiry service, which was first launched in 1987. Today, VNZ-Link has a user-base of over 5,000 access points throughout the country and is enjoying a steady growth in both the number of subscribers and the level of access.

The key features of the VNZ-Link service are:

- Dial-up, PC-based access to all valuation assessments in all Valuation Rolls.
- Historical Property sales information dating back to the early 1980s.
- Complex searches with multiple criteria such as floor area. capital value or net sale price ranges.
- Easy to use, especially designed for non-computer oriented people.
- Supported by a toll-free help desk during business hours.
- Available 24 hours a day. seven days a week (excluding occasional "down-time" for system maintenance).
- Users subscribe to the service on a monthly basis, receiving an invoice at month-end for information retrieved and time spent on-line.
- Low-cost, easy access to property data, with the average roll enquiry costing $1.45 GST inclusive.

In recent times investigations have been made to see how best the VNZ-Link service should be further developed. This included a VNZ-Link user survey earlier this year, where feedback from users provided helpful suggestions for system improvements.

VNZ itself has a number of computer enhancement projects under way which, when complete, will have a flow-on effect on the VNZ-Link service. The most significant of these are:

I. The introduction of street dictionaries for each local authority will improve street name spelling, and standardising of naming and numbering conventions will assist users in the location of specific properties. A "select your street" option rather than the current "type in street name" approach, may be introduced in due course to increase the user friendliness of the VNZ-Link input screens.

2. VNZ, DOSLI and a number of other organisations are involved with Standards New Zealand in developing a New Zealand standard for the transfer of GIS property data. This should lead to greater standardisation of land information and assist VNZ-Link users as other land information systems go on-line. Search criteria and property descriptions are likely to adopt these agreed standards .

3. The continuing upgrading of postal addresses by local authorities and the introduction of the RAPID postal numbering system in rural areas will assist in the onsite identification of individual properties. This more complete postal address system for properties will be progressively reflected in the VNZ database.

4. The planned introduction of EDE (Electronic Data Exchange) with local authorities will lead to the VNZ valuation roll information being more up to date and accurate.

Further VNZ data enhancements are likely to arise from the Crown LIS (Land Information System) project. This development is involved with the integrating of property information from the main Crown land information holding departments: DOSLI, VNZ, the Justice Department's Land Title Office, and the Maori Land Court. Crown LIS is working towards the automated matching and updating of data and will lead, in time, to an increase in both the accuracy and timeliness of VNZ records.

The following section briefly introduces recent and ongoing developments offering improvement in connection speed, access method and general VNZ-Link efficiency. A faster connection speed is available for users with an appropriate modem to take advantage of it. Telecom New Zealand has recently introduced 9600 bits per second dial-up access to PACNET (the Packet Switching Network). Initially established in Auckland only, it is now available nationwide, with Telecom committed to upgrading the network to handle the increased loading as users switch from the lower speed access methods.

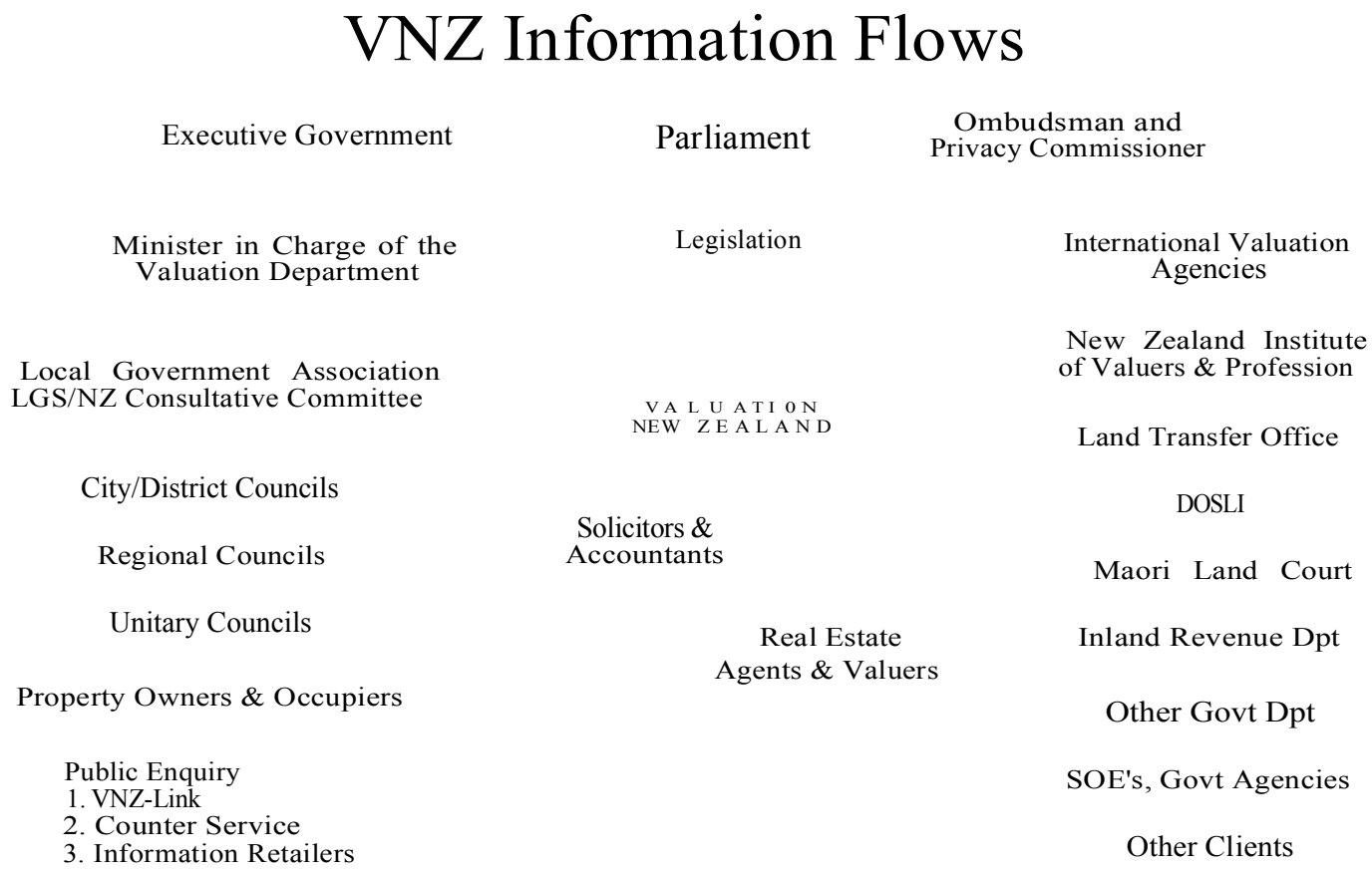
An increasing number of articles are being published on "mobile office" technology. A mobile office, based around a cellphone and notebook or sub-notebook PC, offers a portable method of connecting to other computers or to send faxes, e-mail, etc. At VNZ, we have extensively tested cellular access to VNZ-Link from Wellington, Auckland and Tauranga locations. We have found that using our standard MicroTex communications software, with slight modification, we can reliably achieve online sessions and retrieve data.

Later in the year, VNZ-Link users will have the option of a Windows version of MicroTex from Christchurch-based Hindin Communications Limited. This will assist those who wish to import screens or fields of specific data from VNZ-Link into other applications (word processors, databases or spreadsheets by providing true Windows "cut and paste" functionality. It is also likely to allow "background" connection to VNZ-Link (i.e dialling, connecting and automatic signing on) to occur while the user continues work in other Windows-based applications.

The VNZ-Link service is just one of a series of information flows between Valuation New Zealand and its public and private-sector clients. These information lfows are diagrammatically represented in figure 1. The VNZ database enhancements currently underway, will enable VNZ to better meet the current need for information to support these flows.

The computer systems operated by Valuation New Zealand are based around two networked IBM AS/400 platforms. A diagram of the VNZ computer system, with VNZ-Link highlighted, is illustrated in figure 2.

Figure 1: Diagrammatic representation of VNZ's information Flows.



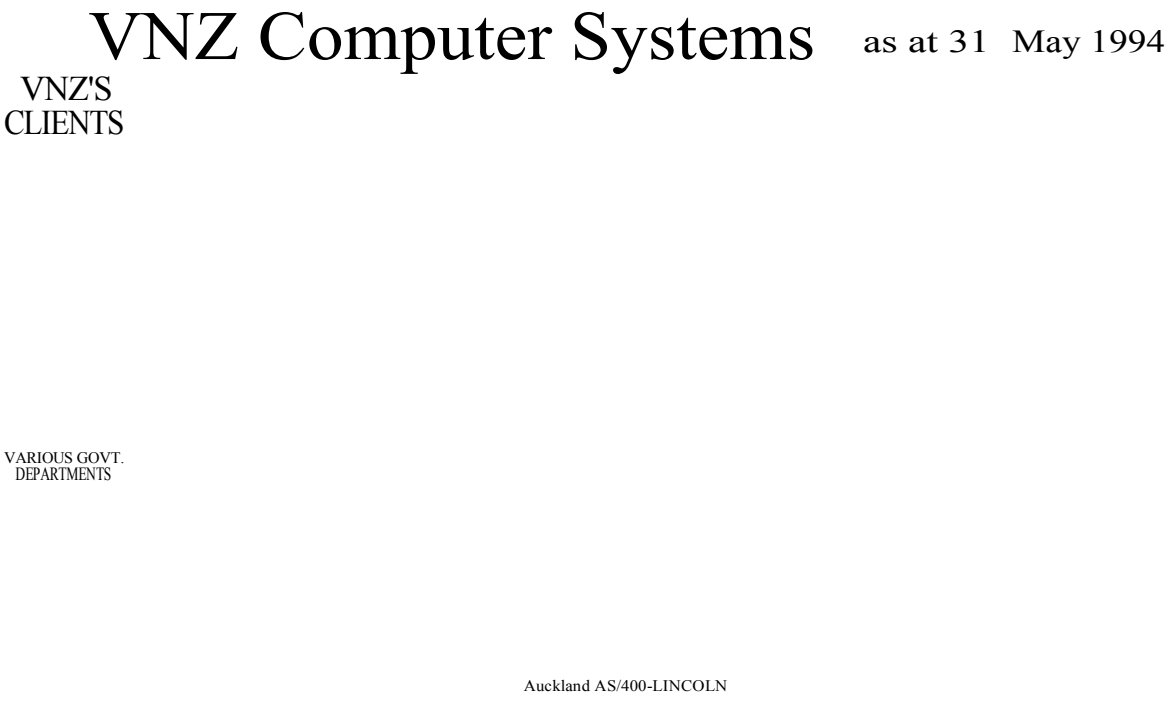


Figure 2:
Schematic of VNZ Computer Systems

Legal Decisions

Rating - Hydro Electric power stations - Ecxlusion of machinery from rateable property - Whether machinery was restricted to moving parts - Whether "fixed to the soil or not" - Separate consideration of each identifiable unit of machinery - Rating Act 1967, ss 2, 3, *5, 7; Rating Powers Act 1988.*

In The Court Of Appeal Of New Zealand
CA 392/92

Between The Otago Central Electric Power Board
Appellant

And The Central Otago District Council
First Respondent

And The Attorney-General
Second Respondent

Coram Richardson J
Gault J
McKay J

Hearing 26 October 1993

Counsel D J More and R M Blake for Appellant

F B Barton for First Respondent

Miss Ailsa Duffy and Miss Brenda Heather for Second Respondent

Judgement 7 December 1993

Judgement Of The Court Delivered By Richardson J

This is a rating case. The central issues on the appeal concern the interpretation of the provisions of the Rating Act 1967 excluding machinery from rateable property and their application to the electric power stations of the Otago Central Electric Power Board in the Tuapeka County in the relevant years ending 31 March 1987 and 1988.

The rates at stake total only $28,754.70 plus penalties and interest. However, the issues are regarded as important and we heard extensive argument not only on the central issues but also on the validity of various steps taken and not taken by various parties and on claims in negligence against the Attorney-General in respect of valuation of land questions. The question is complicated by the restructuring of local and central government. But on the central issues there is no need to go into any of those questions. It is sufficient to record 2 points. The first is that the Central Otago District Council assumed the relevant rights and responsibilities of the Tuapeka County Council on the latter's demise. The second is that when Electricorp and other newly created SOEs were becoming liable for rates in respect of lands previously vested in the Crown a proviso was included in the exclusion of machinery paragraph in the new Rating Powers Act 1988 in these terms:

> "Provided that, in the case of a hydro-electric power station, the term "machinery" shall include only the turbines, the generator and associated equipment through which electricity produced by the generator passes."

While important for rating purposes for all hydro electric power stations for the years affected by the new Act the legislative change does not affect the legal position of the Power Board under the 1967 Act in the years in question.

The statutory exclusion

Capital value system rating was in force in Tuapeka County for the relevant years with rates being made and levied on the capital value of rateable property(s7). Except as otherwise provided in the Act "all land shall be deemed to be rateable property"(s3) but the lands described in the First Schedule are deemed not to be rateable property (s5(1)). Land is itself defined in s2 as meaning "all land, tenements, and hereditaments, whether corporeal or incorporeal, and all chattel or other interests therein, and all trees growing or standing thereon." Except for para 18, all the paragraphs in the schedule concern lands used for specified purposes vested in specified institutions. Paragraph 18 simply states:

> "18. Machinery, whether fixed to the soil or not."

That exclusion dates back to the Rating Amendment Act 1896 s6 of which provided:

> "Notwithstanding anything contained in "The Rating Act, 1894," or any amendment thereof, machinery. whether fixed to the soil or not, shall not be deemed to be improvements, nor shall it be "rateable property" within the meaning of "The Rating Act, 1894", or any amendment thereof.

Moveable chattels are not land for rating purposes but in the absence of an exclusionary provision a chattel which becomes fixed to the land may lose its character as a chattel and become part of the land. The exclusion of machinery provision was recast in the Rating Act 1908 in the same form in which it was re-enacted in the Rating Act 1925 and again in the Rating Act 1967. Between the decision of the Supreme Court in *Grey County v Grey Electric Power Board* [1936] NZLR 247 on which the present appellant relies and the repeal of the 1967 Act there were a number of amendments to other paragraphs in the definition of rateable property in the 1925 Act and in the First Schedule to the 1967 Act respectively but none to the machinery exclusion paragraph.

The factual background

The Power Board has several power houses in the Teviot River catchment area. It occupies a block of 7.2843 hectares and the dams, power houses, pipelines and races are spread over a distance of 7 or 8 kilometres. It was not created as an integrated scheme and the work involved was undertaken over more than a century. The characterisation for rating purposes of what is included in the present overall scheme requires some analysis of the various elements and how it came about. Water race construction by gold miners began in the Teviot area in the 1860s. An 18 foot high dam was constructed in the Teviot River in 1890 to create Lake Onslow. It was added to on a number of occasions over the next 50 years bringing the height to 26' 9".

In 1920 the Teviot Electric Power Board was formed. It acquired various water rights and plant. In 1924 it developed a

combined irrigation and power scheme. Irrigation water is drawn and at times of the year is still drawn from what is known as Ewing Race comprising a Government dam on the Teviot River, tunnel and race originally constructed by a gold mining company. The dam was some kilometres downstream from Lake Onslow which was also used for irrigation purposes.

The first electricity generation installation was the George Power House fed by a pipe from Ewing Race. It was opened in 1924 with 2 machines of 125kw using 25 cusecs of water. The balance of 99 cusecs was used for irrigation purposes. In 1926 a third machine of 600kw was installed. In 1956 the Government completed a longer (1600 m) tunnel from the Government dam on the Teviot River which joined into the existing water race further down.

Between 1938 and 1956 various proposals were made to increase the size of the combined irrigation/power scheme. In 1960 the Teviot Electric Power Board amalgamated with the Otago Central Electric Power Board.

In 1966 there were some changes at George Power House. Then in 1972 the Teviot Bridge Power House opened. Previously the outflow from the George Power House discharged through a long pipeline of 1.1 kilometres into the Teviot River. The Teviot Bridge Power House with a 1125kw capacity was constructed close to the Teviot River.

Between 1978 and 1982 the Power Board constructed the Teviot A and B schemes and built a new dam at Lake Onslow. That dam was constructed in 1982 and at some point a small turbine/generator was installed in a building 3 x 2 in by the dam.

The Teviot A scheme consisted of a headpond constructed in a natural depression near the inflow pipe of 800m to the George Power House and a penstock running from the headpond to Teviot Bridge where another power house (Ellis Power House) was constructed alongside the Teviot Bridge Power House. The Ellis Power House has two 3400kw machines. The Teviot B scheme was a considerable distance upstream. The Marslin Dam on the Teviot River feeds water through a 2.6k concrete pipeline to a new power house (Michelle Power House containing a turbine/generator rated at 1700kw). The outflow from the power house flows through a new water race into the old Ewing Race and thence into the new headpond.

Irrigation water is drawn from the outflow from the Michelle Power House over the dry season between 1 September and 20 April.

Apportionment of capital value

The capital value of the Power Board's property for the years in question was $4m (land value $15,000 and improvements $3,985,000). The initial valuation by the Valuer-General was in 1985 and it seems from researches of counsel that the turbines and generators were excluded from the improvements and not included in that capital value. Then in 1987 and on the assumption that all the works referred to were machinery the Valuer-General determined that $1.8m of the $4m was to be deducted as non-rateable. The rates levied were not altered for the years in question.

The judgment in the High Court

Holland J concluded that but for the decision of Northcroft J in *Grey County v Grey Electric Power Board* he would have had no hesitation in concluding that "machinery" for the purposes of the Rating Act 1967 was restricted essentially to "moving parts". In his view the purpose of the exception was to exclude machinery in the popular sense brought on to the land for a particular manufacturing process which machinery might lose its character as a chattel by virtue of becoming fixed to the land.

Nevertheless for precedent reasons he considered he should follow the *Grey County* decision unless persuaded it was wrong in law. In the *Grey County* case Northcroft J had rejected a submission for the County that "machinery" should be restricted to the moving parts, ie effectively the turbines and generator, and held that a dam, the pipes or conduit conveying the water to the turbines, the surge chamber through which it passed, the turbine and generator, the scroll-case and draught tube which led the water from the turbines to the tail race, and the tail race itself were all "machinery" for the purposes of the Rating Act.

On analysis of the judgments of this court in *Auckland City Corporation v Auckland Gas Company Limited* [1919] NZLR 561 on which Northcroft J had relied, Holland J concluded that they did not support Northcroft J's approach. He also considered that the subsequent decision of this court in *Hutt Valley Electric Power Board v Lower Hutt City Corporation* [1949] NZLR 611 supported the approach which he favoured.

Machinery

The physical resources used in an industrial process may be classified in various ways. There is a well recognised distinction between the location or setting in which business activity is carried on and the apparatus with which it is carried on *(Commissioner of Inland Revenue v Waitaki International Limited* [1990] 3 NZLR 27). But while land and buildings are ordinarily simply part of the setting in which work is performed, in some cases land may be modified and buildings constructed so that they become part of the particular manufacturing or industrial process. Next, descriptive terms such as tools, implements, equipment, machines, machinery, appliances, plant, buildings and land refer to particular resources utilised in the process. Each is descriptive of the particular use to which the object is put, the purpose which it serves. While there is some overlap there are different shades of meaning as reflected in the common use of composite expressions such as plant and equipment or plant and machinery. There are obvious dangers in drawing on discussions of the meaning of any expression other than the term employed in the statutory provision under review.

"Machinery" is defined in The Oxford English Dictionary (2nd ed) as "Machines, or the constituent parts of a machine taken collectively; the mechanism or `works' of a machine or machines." In Webster's Third New International Dictionary it is "machines as a functioning unit...the constituent parts of a machine or instruments." The relevant meaning of "machine" in Oxford is "An apparatus for applying mechanical power, consisting of a number of interrelated parts, each having a definite function... Any instrument employed to transmit force, or to modify its application", and in Webster "an assemblage of parts that are usually solid bodies but include in some cases lfuid bodies or electricity in conductors

and that transmit forces, motion, and energy one to another in some predetermined manner and to some desired end."

The Rating Act is general legislation affecting owners and occupiers of land throughout the country. It is not expressed in technical language. There is nothing in the subject matter or in the statute to justify departing from the ordinary and natural meaning of machinery.

In the Rating Act context it is the lands described in the First Schedule that are deemed not to be rateable property (s5(1)) and the exclusion of "machinery" in para 18 assumes that what was to be excluded would otherwise come within the meaning of "land". The added words "whether fixed to the soil or not" are crucial. To become a fixture a chattel has to be affixed to the land. That assumption underlies the added words. In our view the paragraph is directed to physical items which had the character of machinery before or when fixed to the soil. It is something other than the land. Clearly a natural watercourse such as Teviot River or a lake, pond or water race created or affected by human intervention cannot sensibly answer that description.

In determining the application of para 18 it is also necessary to identify the entity for consideration. The language itself, "machinery, whether fixed to the soil or not", suggests that each identifiable unit must be considered separately. That does not involve a piecemeal approach in which components of an integrated operation are treated separately. On the other hand functionally separated or geographically dispersed items must be looked at separately. To say that they are all part of current business operations does not satisfy the statutory focus.

Machinery: New Zealand cases

In *Auckland City Corporation v Auckland Gas Company Limited* the gas company had constructed gas works in Auckland and had laid its mains and pipes under the streets. The City claimed that the mains, pipes, gasometers and governors were rateable property. By a majority (Chapman, Sim and Hosking JJ, Stout CJ dissenting) the court held that gasometers and governors were within the machinery exclusion but mains and pipes were not. The majority judges concluded that in public legislation of this kind machinery was to be given its popular meaning and that it was necessary to examine the various appliances and consider the functions of each.

Chapman J said at p584:

> "It may be that it [the Legislature] only had in contemplation machines fixed and movable, but machines in a popular sense - that is to say, appliances for transmitting, regulating, or modifying power, and not further including all kinds of appliances used in transmitting the products of factories, though such appliances are connected with machinery. In such a case a popular test is a fair test, and I feel myself unable to say that such fixed things as the mains laid and used for supplying gas are parts of a machine or are properly included under the term "machinery".

Turning to the various appliances he concluded that the gasometers did "actually and actively perform mechanical functions' and the governors were "appliances for modifying a force" but the supply mains "contribute no action" and the main leading to the governor was "not a machine actively contributing to the state of compression of the gas as the gasometer is".

Sim J at p586 said that in its popular meaning machinery:

> "means primarily a number of machines taken collectively, and a machine in its popular sense is a piece of mechanism which, by means of its interrelated parts, serves to utilise or apply power, but does not include anything that is merely a reservoir or conduit, although connected with something which is without doubt a machine. Are, then, the company's gasometers and mains machines or machinery in the popular sense?"

Answering his own question he concluded that:

> "the gasometer performs the function of a pump in connection with the distribution of the gas, and for that reason it may be regarded as a machine. The mains and pipes, however, do not perform any such function in connection with the distribution. They are used in conveying the gas in the first place from the point of manufacture to the gasometers, and from the gasometers to the consumers. They are thus conduits and reservoirs, but nothing more."

After referring to a number of dictionaries and engineering treatises, Hosking J at p590 said that the assemblage of mechanical contrivances at the gasworks was clearly machinery:

> "The whole is a combination of mechanical parts by which motion and force are applied to the production of gas in a merchantable state, including in that the addition of the requisite pressure at the point of exit. To this end it is plain that separate and unconnected gas-pipes do not contribute, and being separate and unconnected they could not, according to the definitions given, be deemed mechanical and come under the designation of "machinery"."

In *Hutt Valley Electric Power Board v Lower Hutt City Corporation* the court applied the reasoning of the majority in the *Auckland Gas Company* case in holding that the poles, cross-arms, insulators and wires used by the Power Board for the transmission of electricity were not machinery within the Rating Act exception. The only reference to *Grey County v Grey Electric Power Board* was by Finlay J. Earlier he had distinguished the case before the court where a construction, i.e. the transmission apparatus, did not invoke force or power and merely acted as a means of transmission of the product to operations performed elsewhere from a case where the whole construction was a unit designed to invoke and use power. At p626 Finlay J noted that *Grey County v Grey Electric Power Board:* "does not conflict with the views here expressed. It is merely an example of the application of the principle here again enunciated, and there is no necessity to consider the validity of the application." In short, it was on the basis that Northcroft J had treated all the items as integrated components of a single entity that Finlay J accepted that the Judgment did not conflict with the views expressed in the *Auckland Gas Company* and *Hutt Valley Electric Power Board* cases.

This brings us to *Grey County v Grey Electric Power Board.* Northcroft J described the case in this way (PP 249-250):

> "the system upon which the works have been constructed has involved, in the first place, the construction of a dam whereby the water of a stream is impounded to be made use of for the purposes of generating power. From the dam the water is led by a conduit or pipeline, part of which is tunnelled through a hill and another part of which is carried across the stream below the dam upon piers. At this point the upper surface of the pipe has been flattened so as to form a bridge used exclusively in connection with the works. The fact that the pipeline is also a bridge is thus only accidental, and its existence does not affect the question for consideration by me. At the end of the pipe-line, the water, before it is led to the turbines, enters a surge chamber intended to equalise pressure. It was explained in evidence that the potential energy in the impounded water - i.e., the force of gravity - is contained by the reservoir and is led by the conduit through the surge chamber to the turbines. This potential energy is turned into kinetic energy by conducting the water through the conduit and surge chamber, thus obtaining velocity. From the surge chamber the water is passed through the turbines, being the part of the machine designed to rotate. Thus the kinetic energy is taken from the water in the resistance offered to its lfow by this part of the machine. The turbine is contained in a scroll-case which also forms the foundation of the power-house, whence the water passes through the draught-tube and the tail-race, thus providing the further fall of water necessary for the performance of its task of generating power."

At p253 he concluded that all the items did

> "constitute a collection of "appliances for transmitting, regulating, and modifying power," and is "a piece of mechanism" which by means of its interrelated parts, serves to utilise or "apply power," and is "a combination of mechanical parts by which motion and force are applied to the production of"electricity in a merchantable state."

The judge accepted that in a popular sense neither the dam nor the tail race would be referred to as machinery but concluded that on proper examination of the subject and after due consideration the ordinary business man or plain man would say that having regard to the definitions which he had cited from *the Auckland Gas Company* case, the whole of the plant of the Power Board was machinery. Northcroft J could not, we think, have reached that view had he not concluded that everything from dam to tail-race was part of an integrated process performing the task of generating power. And he had earlier compared the situation before the court with a steam locomotive and had noted the argument "that as all the component parts referred to about a railway locomotive would be collectively referred to as machinery, so also should the component parts of this plant be thus described."

Conclusions

Like Finlay J in the *Hutt Valley Electric Power Board* case we do not find it necessary to consider the validity of Northcroft J's application of the principle established in the *Auckland Gas Company* case - and affirmed in the *Hutt Valley Electric Power Board* case. This is because the present case is clearly distinguishable on the facts. But, to the extent that some analogy may be drawn between the project in the *Grey County* case and limited parts of the appellant's scheme, we prefer the approach taken in the *Auckland Gas Company* case.

Although understandably now described as the Teviot Power Scheme the history of the work carried out at different times over more than 100 years and the different functions now performed at different and separated locations make it impossible to treat it all as a single unit. It is necessary to examine each item and its function separately as was done in the *Auckland Gas Company* case.

Lake Onslow was created and a dam built for that purpose long before electricity generation was in contemplation. A replacement dam was built in 1982. Associated with it is a small turbine/ generator. Turbines and generators apply motion and force in the production of electricity and qualify as machinery. The lake itself and the dam are essentially for the storing of water and neither transmit nor modify motion and force.

The Marslin dam was simply a reservoir. The pipeline from there to the Michelle Power House diverts water from the Teviot River and, relying on gravity, conveys and confines it in its passage to the power house. The means by which the water is conveyed cannot be described as machinery where the means itself contains no element of motion or action *(Hutt Valley Electric Power Board* case per Hutchison J p637). As in the *Auckland Gas Company* case the fact that the pipe is connected to a machine does not convert it into machinery. The generator/turbine at Michelle Power House is machinery but the outflow pipe and the Ewing race which carry the water a further distance to the head pond are simply conduits. They do not utilise or apply power. The head pond is another reservoir and indeed is also used for irrigation purposes. So, too, in effect are the inflow race and pipeline. The pipelines from the pond to the George Power House and on to the Teviot Bridge Power House and the penstock convey water. They do nothing themselves.
On this analysis generators and turbines at the George, Teviot Bridge and Ellis Power Houses are machinery as are the generator and turbine at Lake Onslow but the dams, pond, pipelines, water races and penstock do not qualify.

It follows that on the central issue the Power Board must fail. On the assumption accepted by counsel for the Power Board that the generators and turbines were not included in the calculation of rateable property on which the rate demands were based, no adjustment to the rates demanded is now required.

In the result it becomes unnecessary to consider all the other issues canvassed in argument. The appeal is dismissed. The first respondent is entitled to costs against the appellant which are fixed at $3,500 together with all reasonable disbursements including travel and any accommodation expenses of counsel. If any question of costs arises in relation to the second respondent counsel may submit memoranda.

Solicitors:

Bodkins, Alexandra, for the Appellant
Caudwells, Dunedin, for the First Respondent

Lease - Interpretation of terms of sub-lease - Sub-lease of office building - No review of rent by sub-lessor/defendant - Plaintiff requested advice of current market rent - Sub-lease contained no "Ratchet" clause - Whether demise clause required defendant to state its assessment of the current market rent and to fix same - Whether triggering of the review process at the option of the defendant - Judicature Act 1908. s 24C (4)

In The High Court Of New Zealand

Auckland Registry
Commercial List

C.L. 56/93

Under Section 24C of the Judicature Act 1908

Between National Mutual Life Association Of Australasia Limited

Plaintiff

And Australian Mutual Provident Society

Defendant

Hearing: 16 December 1993

Counsel: R.J. Craddock Q.C. and T. Sissons for plaintiff
A.D. McKenzie and S.D. Galloway for defendant

Judgement: 16 December 1993

(Oral) Judgment Of Barker J

This is an application under S.24C(4) of the Judicature Act 1908 for the determination by a Commercial List Judge of a question of interpretation of a commercial document.

As noted in other recent occasions when this subsection has been invoked, the Court is usually able to provide for speedy determination of such questions. This case is no exception. The proceedings were instituted only some 2 months ago; counsel have co-operated as to necessary documentation.

The dispute concerns the construction of a memorandum of sub-lease dated 11 June 1990 between the defendant as sub-lessor and the plaintiff as sub-lessee of a property known as General Finance House situated in central Wellington. The sub-lease was for a term of 13 years 9 months, commencing on 1 March 1991 and expiring at 12.p.m. on 30 November 2004. The demise was expressed in these words: "at a yearly rental (hereinafter called "the base rent") of $661,669 (plus goods and services tax) for the period from the date of commencement until the 30th day of November 1992 (and thereafter as determined in accordance with the provisions of clause 3.06 hereof)".

The particular argument is over the rental for the period commencing 1 December 1992. By letter dated 30 September 1992, the plaintiff advised the defendant that it had decided not to review the rent on I December 1992. This letter did not bring a response from the plaintiff until 17 May 1993 when the plaintiff advised the defendant that the effect of the defendant's decision not to review the rent left the amount of rent payable from 1 December 1992 undetermined. The plaintiff then requested the defendant to advise what it considered to be the current market rent as at 1 December 1992 for the next 3 years; such advice was the first step in the procedure laid down in clause 3.06 to which reference will shortly be made.

The defendant refused to take any steps to state its assessment of the current market rent as at 1 December 1992, these proceedings followed. It is agreed that the market rent as from 1 December 1992 would be much less than the $661,669 payable from I March 1991.

The question for determination by this Court is what is the basis for the rental payable from 1 December 1992. The answer to this question requires consideration of not only the demise clause to which I have referred but of the following other clauses -

"3.01 Covenant to Pay Rent:
The lessee shall pay to the lessor during the term of this lease the base rent at the rate hereinbefore specified or where increased in accordance with the express provisions of this lease at the increased rate."

"3.06 (a) Rent Reviews:
At any time not earlier than four (4) months (in which regard time shall not be of the essence) prior to each of the successive dates stated in Item 3 of the first schedule (each of such dates being called "the review date") the lessor may give notice in writing to the lessee setting out the amount which the lessor considers to be the current market rent of the land and the buildings as at that particular review date and unless within one (1) month after the date of service of the said notice the lessee shall by notice in writing to the lessor (herein called "the lessee's notice") dispute the rent so fixed and set out in the lessee's notice the amount which the lessee considers to be the current market rent of the land and the buildings as at that particular review date then the rent so fixed by the lessor shall be the base rent as from that particular review date in substitution for the amount specified in this lease or where applicable the rent determined at any previous review date PROVIDED ALWAYS that notwithstanding that the lessee may dispute the lessor's notice of the current market rent pending determining of the current market rent either by negotiation or as provided in clause 3.06(b) the lessee shall pay base rent for the land and the building at the current market review date SUBJECT ALWAYS to adjustment between the parties once determination by negotiation or pursuant to clause 3.06(b) is completed, such adjustment to include the payment of interest by the lessor to the lessee on any amount refunded to the lessee once the base rent has been determined such interest to be at the rate the lessor is then charging for commercial loans secured by a first mortgage of land."

The remainder of clause 3.06 provides detailed machinery for the fixing of "base rent" after a triggering notice has been given by the lessor. The procedure is fairly often encountered by the Courts in rental disputes; the lessee is required to state whether it agrees with the lessor's assessment of rent and, if not, to state its assessment. The parties are then required to negotiate to resolve the dispute. If they cannot, there is machinery for each to have a representative and for an umpire to be appointed if the representatives cannot agree. There is no need to state these provisions because they are not in issue and the process has yet to be triggered. The most important thing about this document is that it does not contain in actual terms what is commonly called a "ratchet" clause. The effect of such a clause, found frequently in commercial leases, is that, at any rent review the rent for the renewed term cannot be less than that currently being paid. So that if there were a ratchet clause of the commonly understood type, the $661,669 would be the minimum rent payable regardless of what the market rent might happen to be at any given review date.

One could take judicial notice that these

parties, both prominent in the New Zealand commercial property market, would have been aware of the desirability or otherwise at a ratchet clause. In fact clause 2.04 of the document provides a limited ratchet clause; it relates to the rental payable on a renewal of the lease when the lease finally expires in 2004. The lease was adapted from standard leases of the defendant and of an organisation known as "SOMA New Zealand". I pay little regard to those other documents because this document has to be construed within its four corners; but it is legitimate to assume as part of the factual matrix that these parties decided for whatever reason that they would not have a ratchet clause in their lease.

The simple submission of the plaintiff is that despite the permissive wording of S.3.06(a) the demise clause requires the lessor to state its assessment of the current market rent as at 1 December 1992 and thereafter to go through the extensive process for fixing current market rent as stated in the remainder of clause 3.06. The submission is based on the fact that "base rent" is defined by the lease as being "the yearly rentals" (hereinafter called the "base rent") which is fixed at a named amount from the date of commencement of the lease until 30 November 1992 at $661,669. The plaintiff's submission is that, thereafter, the "base rental" falls to be determined in accordance with the provisions of clause 3.06. Indeed, reference to clause 3.06 shows the new "base rent" is the product of the review process "in substitution for the amount specified in this lease or where applicable the rent determined at any previous review date".

The submission of the defendant is that clause 3.06(a) clearly makes the triggering of the review process purely at the option of the lessor. Had the tenant wanted the right to trigger the review process itself, then it should have ensured that the right to trigger the review was given to both parties. The defendant submitted that the wording is clear that the triggering of the notice is completely optional in the discretion of the defendant lessor.

Counsel for the defendant pointed to clause 3.01; in particular, counsel relied on the words "or where increased in accordance with the express provisions of this lease at the increased rate". The effect of the submission was to make clause 3.01 a de facto ratchet clause because there was no way in which "base rent" could be reduced, should the lessor elect not to trigger the process under clause 3.06.

The matter is fairly finely balanced but, as with all commercial contracts, I must endeavour to ascertain the intentions of the parties from the words used and I must consider a commercial solution to the problem posed.The lease document itself' is not particularly happily drafted. I suspect that this was because the drafter was somewhat unselective in what parts of the BOMA or previous AMP leases were adapted for use in this document which signally failed to contain the usual ratchet clause.

In my view, the central and dominant provision of any lease must be the demise clause. The parties have gone to some lengths to specify that the $661,669 rental figure applies only for the specified period. They have gone on to specify what the yearly rental, i.e. "base rent" should be thereafter and to invoke the machinery of clause 3.06. On the face of it, that machinery can be triggered only at the election of the lessor; but to ascribe that construction would be to render meaningless the demise provision. To give the demise provision some meaning, the parties must be taken to have assumed that the lessor should give the notice in writing triggering the review process and with that notice should have stated the lessor's view of the current market rent. At the very least, it must be that the lessor is required to trigger the process should the lessee require it.

I cannot read clause 3.01 as being contrary to that view; the expression "base rent at the rate hereinbefore specified" rather begs the question as to what the base rent should be; the answer to the question - "what is the base rent?" must determined by looking at the demise provision.

I am heavily influenced in my decision by the deliberate decision of the parties not to include a ratchet clause. I feel that the submissions of the lessor in this case would have the result of including a ratchet clause where the parties have deliberately gone out of their way not to include one. Although there is the permissive word "may" in clause 3.06, I do not think that word can sit happily in these circumstances with the clear wording of the demise clause. At worst, as counsel for the plaintiff submitted, there is a minor gloss on clause 3.06 in these circumstances.

Although the equity of the situation does not matter, the reality is from this interpretation that the lessor will still be obtaining a market return on its investment.

The matter is in very short compass. For the reasons I have endeavoured to express, there will have to be judgment for the plaintiff. No doubt counsel can agree on the terms of a suitable declaration. The plaintiff is entitled to costs. I shall hear counsel if need be. Liberty to apply on costs is reserved.

Solicitors:

Simpson Grierson Butler White, Wellington, for plaintiff

Rudd Watts & Stone, Wellington, for defendant

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ISSN 0113-0315