IN THE MATTER of the Arbitration Act 1996

AND

IN THE MATTER of The Maori Reserved Land Amendment Act 1997

AND

IN THE MATTER of a rent review

BETWEEN **THE PROPRIETORS OF PARININIHI KI WAITOTARA BLOCK**, A Maori Incorporation in terms of the Te Whenua Maori Land Act

Lessor

AND **THE LESSEES NAMED** in the First Schedule to an Arbitration Agreement executed between the parties

Lessees

AWARD OF SOLE ARBITRATOR
THE HON. SIR IAN BARKER QC

Hearing: New Plymouth, 12, 13, 14, 15 and 16 May 2003
Auckland, 20 May 2003

Date of Award: 17th June 2003

Counsel: Mr Justin Toebes for Lessor
Mr Nicholas Davidson QC for Lessees

Solicitors: Buddle Findlay, Wellington for Lessor
Welsh McCarthy, Hawera for Lessees

INTRODUCTION

1. In the province of Taranaki and in the Waverley/Waitotara district, are found some 313 holdings of Maori reserved land, held by lessees under perpetually renewable leases. Most of the holdings are used for dairy farming, some for dry stock or grazing. The current owner of the freehold of all these holdings (which have a combined area of some 20,000 hectares) is the Lessor in these proceedings, "The Proprietors of Parininihi Ki Waitotara Block" (**"the Lessor"**). This body is incorporated under Maori land legislation and administers the leases on behalf of numerous Maori owners who own shares in the Lessor. The leases are often referred to as "West Coast Settlement Reserve Leases" or "West Coast Leases".

2. 289 of the Leases are owned by members of the West Coast Settlement Reserve Lessees' Association Incorporated (**"the Association"**). The Lessor and the Association each appointed a registered valuer in an endeavour to agree on the rentals payable to the lessor by each lessee at a rental review, due for most of the Leases to occur on 1 January 2003. The valuers so appointed are both highly experienced in rural valuations, especially of Taranaki dairy farms. They are Mr RS Gordon for the lessor and Mr JP Larmer for the Association.

3. In their deliberations over what should be the fair annual rent payable by each lessee to the lessor over a period of 7 years commencing 1 January 2003, the valuers sensibly came to agreement on several important matters, which shall be described later. They were unable to agree on the fair annual rentals. The parties agreed that this Arbitral Tribunal should determine the rent payable under some 30 representative Leases. 30 representative lessees have signed the Arbitration Agreement agreeing to be bound by the arbitration and allowing the Association to represent each of them in the proceedings. The valuers are confident that, once the views of the Arbitral Tribunal on the 30 representative leases will have been known, then they will be able to reach agreement on the fair annual rent to be paid by the 259 other lessees who are also members of the Association.

4. The Arbitration Agreement appointing the Arbitral Tribunal was signed by the lessor on the one hand, and the Association on the other, representing the 30 named lessees named in Schedule 1 hereto. The Lessor and the 30 lessees named in Schedule 1 are the parties to this arbitration. In addition, there are agreements between the Association and those members of the Association not named in Schedule 1, that they will accept the ruling of the Arbitral Tribunal in respect of the 30

named lessees and that they will, thereafter, accept the joint determination of the valuers who will fix rentals for their leases based on the precedents established in the Award for the 30 representative Leases. It is anticipated that the valuers, who reached a laudable and, indeed, exceptional measure of agreement prior to the arbitration, will be able to fix the rentals for the Leases of these other members of the Association without resort to further arbitral proceedings.

5. The situation with regard to the 24 Leases owned by persons who do not belong to the Association is unclear. The lessor is dealing directly with them in terms of the relevant legislation. Once rentals have been fixed for the 30 indicator leases, it may be possible for the lessor to reach consensus with these other lessees. Under the Arbitration Agreement, the task of the Arbitral Tribunal is to fix a rental in respect of each of the 30 named properties. The Arbitral Tribunal must have regard to the relevant legislation (to which reference will later be made) and to those principles of valuation methodology considered to be applicable.

6. 248 of the 289 Leases belonging to members of the Association have a rent review date of 1 January 2003. 12 have an earlier date. 29 have a later date. No difficulty is anticipated by the valuers in dealing with these minor variants, once the Award has been issued. They have agreed on appropriate values where the rent review date was earlier than 1 January 2003, but not where the rent review date was after that date.

7. The parties have agreed to the payment by the lessees to the lessor of rental from 1 January 2003 on a particular basis. This arrangement is without prejudice, either to the rentals set by this Award, or to those set subsequently by the valuers in consequence of the Award. Appropriate adjustments will be undertaken by lessor and lessees in respect of payments made under this transitory arrangement.

HISTORY

8. The history of the Taranaki West Coast Leases is long, involved and not free from tensions. There are identical leases of rural land in the West Coast of the South Island which are held under the same legislation. The history was referred to by both valuers in their evidence. It must be well-known to the parties, so that it does not need detailed repetition in this Award. Legislation, litigation and commissions of enquiry have ranged over more than a century. The interested reader can refer to a 1996 Court of Appeal decision which describes the early development of West Coast

leased lands and records some of the events leading to legislative changes over the years: see *The West Coast Settlement Reserves Lessees' Association Incorporated v Valuation Appeal Committee and Others,* reported in NZ Valuers' Journal, July 1997.

9. The West Coast Leases granted in the 19th century were initially terminating. In 1892, the Government of the day enacted the West Coast Settlement Reserves Act 1892 which set up a perpetual leasing regime with 21 year rental renewals. The lessees at that time paid a capital sum for improvements, which, under previous arrangements, would eventually have reverted to the lessors. Under the 1892 Act, the lessees were henceforth to own all improvements. The Public Trustee administered the Leases for Maori owners. The rent for each 21-year term was set at 5% of the "residual value", being the gross value of the property less the value of improvements. The Native Trustee replaced the Public Trustee in the 1920s. Considerable dissatisfaction by lessors at the level of rental income caused the setting up of a Royal Commission (the Myers Commission) in the 1940s. The result of the Commission's report was an amendment to the 1892 Act in 1948. This amendment was followed in 1955 by the repeal of the 1892 Act. Its consolidation became the Maori Reserved Land Act 1955 (**"the 1955 Act"**). In accordance with the recommendation of the Myers Commission, the 1948 and 1955 Acts fixed the rent of West Coast leases at 5% of the unimproved value of the land based on a special valuation, with a right of objection to a Valuation Appeal Committee established by the Act. The change made to the rental assessment criterion was from residual value to unimproved value.

10. Some 126 Leases were freeholded over a period until 1973, when the then Minister of Maori Affairs initiated a policy which saw no further freeholdings. In 1962, the Maori Trustee amalgamated the titles of the West Coast Settlement Reserves, giving the beneficial owners shares in the whole of the lands, as distinct from owning individual interests in particular sections. Freeholding by lessees is still technically possible under present legislation but is subject to statutory provisions which make it difficult to achieve in practice.

11. A further Commission of Inquiry ("the Sheehan Commission") was later set up because the Maori owners considered that the 21-year lease period, without any intermediate rent review, was unfair to them during periods of high inflation. The Sheehan Commission reported in 1975. Legislation followed in consequence,

authorising the establishment of incorporations of owners as bodies corporate. Reserves could be transferred to such incorporations by the Maori Trustee. The present lessor, created as a Body Corporate under the relevant legislation, has been the owner and lessor of the West Coast Leases since 1977. Besides receiving the West Coast lease rentals, it owns several farms in its own right. Amongst other activities, it maintains an enlightened programme of fostering educational opportunities for young people.

12. In 1991, the Ngai Tahu Report of the Waitangi Tribunal made a number of criticisms of the 1955 Act (as it applied to land on the West Coast of the South Island). Yet another report on West Coast leases was commissioned, the "Marshall Report". This recommended major changes to the statutory lease contract as set out in the 1955 Act. An Amendment Act in 1997 altered all standard Lease contracts between the lessor and the individual lessees. This Act will be referred to as "the 1997 Act".

13. Lease terms for West Coast leases are of a standard variety, usually found in perpetual leases of rural land. These terms do not need to be set out here. They can be found in a Schedule to the 1955 Act. The lessee must pay rates, outgoings, repairs, insure and maintain buildings and structures on the land and, in general, cultivate the land properly. These standard terms are still in force but all leases are now subject to significant differences to the leasing regime introduced by the 1997 amendment, ie:

(a) The change to 7-year periods between rent reviews instead of 21 years. This change was phased in over 4 years, commencing 1 January 2001. The present arbitral exercise is the first rent review for Taranaki leases under the 1997 legislation.

(b) The granting to the lessor of a right of first refusal on any proposed assignment of the lessee's interest, as opposed to a previously unrestricted right for the lessee to transfer. The legislation is widely-drawn, so as to include assignments to trusts and company share transactions. Transfers to spouse or children were exempted from the first refusal regime, which is set out *in extenso* in the statute.

(c) The change in assessing rent from a fixed percentage of unimproved value to be *"the fair annual rent of land for the next ensuing period of the term of the*

Lease so that the rent is uniform throughout the whole of that ensuing period" (1997 Act Schedule I, clause 4(1)).

14. The 1997 Act also provided compensation and a solatium for both lessors and lessees. These payments were apparently considered appropriate because of the changes to the statutory contracts which the Act effected. Section 16(1) states that lessees at the time of the commencement of the Act are entitled to compensation for:

(a) The change to a more frequent rent review;

(b) The change to a fair annual rental based on the unimproved value of the land; and

(c) The conditions imposed by the Act on the assignment of the lessee's interest.

15. A Schedule to the Act detailed how compensation was to be assessed, with the right of resort to the Land Valuation Tribunal. Section 26 provided for a solatium – one payment per lease – to recognise the justifiable but unquantifiable transaction costs that would be incurred by lessees as a result of the changes to leases made by the Act. The solatium was $500 plus a *pro rata* share of a fund of $2 million. The respective shares in this fund for lessees were to be calculated on the unimproved values of each West Coast lease. The provisions for compensation and solatium for the lessor were in similar, but not identical, terms.

16. In section 3, where the purposes of the 1997 Act are set out extensively, reasons for the above payments are stated. In addition, lessors were to be given funding by the Government to a limit of $6 million to assist in the purchase of lessee interests when they become available. There was to be one payment per lease. Section 28(3) stated that this assistance in providing purchase money for leases recognised that lack of sufficient purchase money had been one of the major factors in the past preventing lessors from purchasing lessees' interests. It was declared to be in the interests of both lessors and lessees that the Crown should make such a contribution. Clauses 26 to 30 of Schedule 1 to the 1997 Act give a right of first refusal to lessees, should a lessor wish to sell any leased land other than to a person who comes within the preferred class of alienees under Te Ture Whenua Maori Act 1993.

17. Under clause 4(2) of Schedule I of the 1997 Act, "land" in clause 4(1) of the Schedule 1 (the rent assessment provision) means land in the state it was for calculating the unimproved value under Part III of the Maori Reserved Land Act 1955. This definition is the same as that for "unimproved value" under the Valuation of Land Act 1951: see s 65(2) of the 1955 Act. The definition is:

> "The sum which the owner's estate or interest therein, if unencumbered by any mortgage or other charge might be expected to realise at the time of valuation if offered for sale on such reasonable terms and conditions that the *bona fide* seller might be expected to impose, and if no improvements (as hereinbefore defined) had been made on the said land."

The 1970 amendment to the Valuation of Land Act 1951 made improvements on the land part of the unimproved value. However that amendment did not apply to perpetual leases such as those under consideration here.

18. All improvements on West Coast leasehold land are owned by the lessees. Only the land in its assumed unimproved state is owned by the lessor. Improvements can be structural improvements, such as buildings, fencing, water access and on-farm infrastructure. These are known as improvements **on** the land. The second category, improvements **to** the land, includes but is not restricted to, clearing, drainage, land preparation, fertility-improvement and grassing. These are also called developmental improvements.

19. The task of the valuers and of this Arbitral Tribunal in ascertaining the fair rent is a highly artificial one. One has to assume that land is in its undeveloped state, ignoring the transformation effected over the years since 1892 in improvements on and to the land. One has also to assume that the existing infrastructure, not on the land, is in place, such as roading, water supply, etc. Some of the subject holdings had originally been covered in bush: some were formerly flax and fern country, with open land being found on and around the coast. Other areas had been cleared by Maori occupants prior to 1892. An old map of Taranaki province, produced at the hearing, shows the bush-line around Mount Taranaki. As European settlement developed, the bush-line steadily receded up the slopes towards the mountain reserve.

20. Schedule 1 of the 1997 Act stipulated the machinery for rent review under the new regime. Mediation was required as a precursor of arbitration. The parties considered that the consultations between the valuers, which had extended over 12 months and which had resulted in agreement over many areas, should be considered as satisfying the requirement for mediation. The parties therefore agreed upon this

present arbitral process, mindful of the draining and costly litigation of the past, in the hope that the Arbitral Tribunal will be able to provide a guide to the valuers in assessing the rentals for all the Taranaki West Coast Leases. In passing, another feature of the 1997 Act worthy of note is the exclusion of any resort by the parties to a state-supplied dispute resolution body (such as a Land Valuation Tribunal) and to a requirement for them to engage in an arbitration process which is the usual vehicle for determining commercial rental disputes.

HEARING

21. The hearing of evidence and submissions in this arbitration took place in the Plymouth International Hotel, New Plymouth over 5 sitting days. Witnesses read prepared written briefs of evidence-in-chief and a full stenographic record was made of supplementary evidence-in-chief, cross-examination and re-examination. All witnesses gave evidence under oath.

22. On 13 May 2003, the Arbitral Tribunal, in the company of Messrs JP Larmer and RS Gordon, the valuers for the parties, made an inspection of such of the indicator properties as could conveniently be visited in the course of a day. Effectively, there was a circumnavigation of the mountain. This inspection was extremely useful to the Arbitral Tribunal in gaining an understanding of the variety of properties involved and their differing land quality. The Arbitral Tribunal is grateful to Messrs Larmer and Gordon for their guidance during the course of an informative day. A view forms part of the evidence: see *Webster v Burns*, [1964] NZLR, 749.

23. Counsel made their final submissions in Auckland at the Northern Club on 20 May 2003. The Arbitral Tribunal is grateful to counsel, not only for their helpful submissions, but also for their efficient conduct of the hearing and their careful preparation of the evidence. To keep this Award within manageable size, the Arbitral Tribunal does not intend to refer to every facet or nuance of the evidence and submissions. However, the parties can be assured that all evidence and submissions have been considered.

24. Representatives of both sides attended the hearing. The Arbitral Tribunal records that, whatever may have been the problems in the past, one sensed at the hearing a sense of co-operation between the parties to achieve certainty from the difficult exercise of rent setting under the new assessment regime.

25. Because this Award will be made available to interested persons, all who read it, from whichever side of the argument, should understand that the current rent-fixing operation is quite different to any process in the past. This is because of the changes to the rent review criteria imposed by the 1997 Act. Consequently, rentals fixed in 1990, under the 1955 Act, may or may not bear similarity when compared with rentals assessed in this arbitration.

26. The parties were indeed fortunate in that each had instructed a highly-respected and experienced rural valuer. As noted earlier, Messrs Larmer and Gordon are to be congratulated for having reached agreement on key issues over the course of almost a year of inspecting almost all the leasehold properties concerned. In addition, they captured relevant information of sales and leasing in Taranaki and considered comparable sales and rental-setting evidence from elsewhere. Both gave evidence with a high degree of professionalism which greatly assisted the process. They produced at the hearing a dossier describing each of the 30 indicator properties in considerable detail. They produced schedules indicating their agreed figures. They provided useful commentary during the inspection by the Arbitral Tribunal.

27. In addition to the valuers, the following further witnesses were called. For the lessor:

(a) Mr AP Laing of Dunedin, Registered Valuer and Chartered Accountant; and

(b) Dr Adolph Stroombergen of Wellington, Economist

For the lessees:

(i) Mr Alan Crighton of Christchurch, Management Accountant and Registered Valuer; and

(ii) Dr Greg Anderson of Christchurch, Economist.

These witnesses, whilst giving helpful evidence, were not as pivotal to the respective cases as were Messrs Gordon and Larmer.

28. The basis for choosing the 30 indicator properties was similar to that adopted by the same two valuers in the 1990 rent review (under the 1955 legislation). The portfolio stretched from Motunui in the North to Waitotara in the South. The selection revealed a mix of land classes from Class I, (top quality, easy contoured fertile

Egmont black loams in premium localities such as the Waimate plains) to Class IV, (poorer quality laharic hummocky in the Rahotu area). There were some 6,000 hectares of grazing or dry stock land. The remainder are dairy farms or parts of dairy farms. The valuers consider that the 30 indicator properties give a representative sample applicable to the individual localities of all the leases, based on locality, land use, soil type, contour and value. The valuers have both had experience of dairy farming. They advise dairy farmers in farm management. Both have been involved in high-level valuation dispute resolution and real estate dealings. Both are Fellows of the Arbitrators' and Mediators' Institute of New Zealand Inc.

29. The areas of agreement between the valuers can be summarised as follows.

(a) **Current Market Value**: The price to be accepted by a willing vendor, from a willing purchaser for the purchase of a farm on the open market, including in the case of dairy land, co-operative shares and capital Peak Notes in Fonterra Co-operative Group Limited ("Fonterra"). In assessing the current market value, both valuers considered evidence of the prices for sales of farms over the previous season. They were able to express values, either on a per hectare value or on a per kilogram of milk solids basis. In most cases, properties were within a 10 to 15 kilometre radius of a particular subject farm.

(b) **Valuation of Dairy Company Shares**: Every Taranaki dairy farmer must own Fonterra shares, based on one share for each kilogram of milk solids obtained from milk supplied from the farm in question in the prior season. The fair value of such shares is set by Fonterra every year. The evidence was that the current indicative fair value for each Fonterra share is $3.95, equivalent to 3.95 kilograms of milk solids. In addition, the farmer must purchase Fonterra Peak Notes at a price fixed by the Fonterra Board, currently $30 per note. In valuing the shares, the valuers either had details of the kilograms of milk solids supplied from the farm to Fonterra or else they determined the average efficient productivity stand for each farm. They used as a benchmark what the number of kilograms of milk solid supplied from that farm would be, where a property was presently used as a dairy farm and for those not presently so used where the highest and best use of the land was for dairying. Some indicator properties had dairying as the highest and best land use but the land was presently used for other purposes (eg racehorse training or maize growing). Fonterra shares are not improvements on or to

the land. Practically speaking, the entitlement to shares is something that has to be transferred on the sale of a dairy farm as a going concern.

(c) **Value of chattels**: Chattels in the buildings on the land, plus milk plant, electric fence unit and the like.

(d) **Capital Value**: Land and buildings assessed, after taking the value of the Fonterra shares and the chattel value from the current market value. This item represents the total value of the land, including improvements to and on the land.

(e) **The Value of Improvements on the Land**: This includes buildings such as house and milking shed plus fences, races and water supply.

(f) **Land Value**: This is the capital value less the value of the improvements **on** the land, based on comparable sales evidence.

(g) **Development Improvements**: Improvements **to** the land comprising clearing of bush or fern flax, grassing application, fertiliser drainage and consolidation. Some are intangible improvements such as the building up of fertility. Those improvements which can be identified as part of an artificial construct do not form an asset, able to be dealt with separately. Therefore, the approach to an assessment of value is not based on comparables or standard costings. The valuers were able to agree on these improvements from their own experience and from reports from farm consultancies and stock firms.

(h) **Unimproved Value**: This is the bare land value, less the value assessed for improvements to the land. This asset is not traded on the open market as such because there is no unimproved land for sale. The assessment was reached by deduction of the other components from the current market value, leaving the residual unimproved value. If there were any bare unimproved land for sale, in Mr Gordon's view, there would be a rush of purchasers to buy it.

(i) **Average Efficient Productivity Expressed in Either Kilograms, Milk Solids, or Stock Units**: Each property has an assessed average efficient productivity which is a matter of judgment for the valuer.

(j) **EBIT** (earnings before interest and tax: The earnings projection has been based on an average of historical date ($4.25 per kilogram of milk solids, recognising the highs of $5.3 per kilogram of milk solids with a projected low of $3.70). EBIT calculations have been completed on the basis of revenue projections for a 50% cost to growth income ratio, based on known sampling of actual results from dairy farmers and allowing wages for management return, based on what the market is paying for dairy farm management.

30. Mr Gordon in his evidence, instanced one property, No 26, to exemplify what had been agreed between Mr Larmer and himself for each property. The valuers were not entirely in agreement over the extent to which the notional lessee of the land in its bare unimproved state would effect, as improvements on the land, the actual improvements found today on any given property. Some properties, for example, were too small to be an economic dairy unit in today's conditions. There was some debate as to whether the notional lessee would build a house or milking-shed on these properties or would seek to combine them with another property. The Arbitral Tribunal does not consider those differences material in the light of the agreements reached as to values. Mr Gordon's example follows, demonstrating how the agreed valuation agreements worked out in practice.

"Land Use : Dairy	*Highest and best land use*
Address : Ohangai	*District locality*
Cover : Open	*Original cover*
Area : 54.68 hectares	*Title area*
Effective area : 52 hectares	*Effective grazable area*
CMV : $1,580,000	*Current market value as assessed from comparable sales data.*
Shares:	*Dairy company shares based on average efficient productivity of 50,000 kilograms of milk solids @ #3.95 per Co-operative share and $30.00 per peak note and $1 per kilogram of milksolids peak note equivalent.*
Chattels:	*Based on an assessment of the value of chattels in the dwelling house, milk plant in the cowshed and other sundry chattels such as feed or non fixable plant.*
Capital Value : $1,300,000	*The value of land and buildings derived from the deduction of the value of Shares and Chattels from the Current Market Value*

Value of Improvements : $250,000 on the land	*The value of structural improvements comprising buildings, fencing, race access and water supply. Assessed by valuer judgment but also with reference to the market. Improvements on the land were jointly agreed on an assessment of the added value of those improvements on the land.*
Land Value : $1,050,000	*The value of land derived after deduction of the value of improvements to the land from the Capital Value*
Development improvements : $290,000 on the land	*Improvements to the land comprising clearing, grassing and consolidation with a margin of cost over development referenced from development costs and Tribunal authorities as to the margin over cost. In this particular case this was open country, original cover fern, flax and tutu with the added value of improvements to the land reflecting the minimal costs of clearing, cultivation and seeding, building up of the fertility along with the time value of development and the margin of value over cost.*
Unimproved Value : $760,000	*The value after deduction of the value of improvements to the land from the Land Value.*
Production (kgs) : 85,000 kgs	*Productivity assessed under an average efficient level of management based on the district norm for the subject property. The productivity assessment under an average efficient level of management has been benchmarked against actual productivity with the appropriate adjustments made for management and other non-standardised factors.*
Current Market Rental (including right to use shares) :$70,000	*The rent applicable to that lease for all components of the current market value assessed using market rentals of comparable properties. This rent has been derived from consideration of the sample of comparable rentals for similar type dairy units on commercial lease terms for three year terms with one to three year rent reviews.*
Rental (per kg) : $1.40 per kg	*The rental divided by the productivity. Generally the rate per*

	kilogram based on average efficient productivity is relatively homogenous for similar type properties within a given locality.
Rate per ha : $1280	*Rent divided by title area*
Rent per effective ha : $1346	*Rent divided by effective hectares*
Rental rate including right to use	
Shares : 4.4%	*Rental divided by current market value*
Ebit	*$70,000*

31. The valuers agreed that the 1997 Act contemplates the determination of a "fair annual rental" by determining the unimproved value and applying a percentage rate thereto.

32. In Taranaki, many freehold market leases are traded on an arm's-length basis. The data obtained by the valuers applicable to these can be extrapolated to the current market rental per hectare or per kilogram of milk solids. The valuers were able to agree on comparable leasings on the open market, including rentals for varying periods with varying covenants either of i) bare land or ii) of land plus improvements plus shares or iii) of land and buildings only. Production and EBIT data were taken into account. Usually, the leases included the right to use Fonterra shares.

33. Consequently, the valuers were able to agree upon the current market rental for the 30 indicator properties including where applicable, the right to use dairy company shares and chattels, improvements on and to the land and the unimproved land, based on a normal rural Taranaki Lease with standard terms. These terms could include some rights of renewal and rights of rental adjustment. Normally, the lessee has to meet all expenses including maintenance, weed control, insurance, rates, and farming costs. The lessor has to assign the Fonterra shares to the lessee for the term of the Lease with reversion at termination if the lessee supplies milk from the property.

LEGAL PRINCIPLES

34. There was little dispute about the legal principles applicable to the present unreal exercise of rental setting. These principles have been developed over the years in the course of many arbitrations and Court decisions over renewals of perpetual leases, both rural and urban. These leases (often called Glasgow leases) are anachronisms from the 19th century. The are unlikely to qualify as desirable

investment vehicles in the 21st century, largely because the lessor gives up so much forever, as soon as the lease begins. Most of the cases, concerned with 21-year rent reviews, demonstrate the inevitable tensions arising between captive parties locked into a relationship which has some symbiotic qualities.

35. Rent reviews every 7 years instead of every 21 years are said to benefit the lessee by reducing the impact of a dramatic increase in rental every 21 years, with all its attendant difficulties for cash-flow and budgeting. Such reviews are said to benefit the lessor who receives rental, assessed more frequently on an increasing land value. Whilst useful dicta have come from the Courts, worthwhile statements of principle can also be found in the awards of distinguished legal arbitrators and umpires who have applied well-known principles to situations such as the present. Whether similar awards issued after 1 July 1997 will receive the same publicity, in view of the confidentiality provisions of the Arbitration Act 1996, is unclear.

36. It is not necessary to over-burden this award with too many statements from the large number of authorities to which the Arbitral Tribunal was referred. Some principles need to be stated in order to signal the legal course which the Arbitral Tribunal must and will follow.

(a) The valuer determining "fair annual ground rent" must ascertain

> "what a prudent Lessee would give for the ground rent of the land for the term and on the conditions as to renewal and other terms, etc mentioned in the Lease".

Drapery and General Importing Co of NZ Ltd v The Mayor of Wellington (1912), 31 NZLR 598, 605. This authority was affirmed by the Court of Appeal in *Granadilla Ltd v Berben* (judgment, 10 March 1999), in *Sextant Holdings Ltd v NZ Railways Corporation* (1993), 21 NZ Conv C 191, 556 and in *S & M Holdings Ltd v Waterloo Investments Ltd*, [1999] 3 NZLR 198.

(b) There is no difference between the criterion of the prudent lessee and one which postulates a willing but not-anxious lessor and a willing but not-anxious lessee (*Sextant*). For every notional prudent lessee, there must obviously be a notional willing but not anxious lessor for the premises on offer who must be assumed to be willing

> "to take a ground rent which a reasonable but prudent lessee thinks fit to give".

In *re A Lease, Wellington City Corporation to Wilson*, [1936] NZLR s110, s113.

(c) The valuer of the ground rent is to be concerned only with matters which would affect the mind, and ultimately the judgment, of the prudent lessee in making the offer of rental to the lessor. Looking at the matter from the hypothetical willing, but not-anxious, lessor's perspective, it is what the lessor can reasonably expect to be offered which must be assessed, not what the lessor would like to receive. *Wellington City v National Bank of New Zealand Properties Ltd,* [1970] NZLR 660, 670.

(d) The best evidence for assessing rental is derived from a consideration of comparable rentals paid on the open market in similar leasing exercises. Because there are no new Glasgow lettings, evidence of comparable rentals is unlikely to be available. In the absence of such evidence, the valuer necessarily has to proceed by an approach which determines comparable rental transactions and a market value for the property. The valuer then applies a percentage appropriate to the circumstances to fix a figure tor the rental to be paid. Perusal of relevant decisions suggests that this approach may have become the predominant method of fixing ground rents on renewals of perpetual leases. This methodology is called the 'traditional approach' (*Granadilla p 4).* The Court of Appeal considered that this approach was usual and available in that case since there was insufficient market evidence of comparable letting. This approach also provides a method of checking an assessment by reference to such lettings (*Granadilla* p 5).

(e) The valuer should preferably begin by considering comparable lettings, making adjustments for differences in time, physical factors (like location, size intervention and lease terms including duration). This is what was called in *Granadilla*, the 'classic' approach. But if, as frequently happens, the valuer reaches the conclusion that there are no or no adequate comparable lettings, the valuer must adopt another approach based on prudent valuation practice. In *Granadilla*, the umpire, felt he had little realistic choice than to apply the

traditional approach. He assessed a value for the land multiplied by rate a of rental. The Court of Appeal did not question this approach.

(f) It is for the valuer alone to decide what market evidence is comparable. The Court will intervene only when it can be said that no reasonable person in the valuer's position could have excluded or disregarded some material (*Granadilla* p 7).

37. In *Granadilla*, the primary Judge considered that the umpire had not erred in placing little weight on new market leases. He was entitled to make a considered choice in favour of one conventional approach rather than another. He was not in error in placing only limited weight on the "classic" approach. He was entitled to find that the market evidence was of limited use, because it was neither directly or clearly comparable.

38. In *S & M Holdings Limited v Waterloo Investments Limited* (*supra*), the Court of Appeal at p 199 adopted with approval the dictum of Williams J in *S.E.G. Holdings Limited v Auckland City Council*, (High Court Auckland, 7 May 1996, unreported). What that learned Judge said is applicable to the present case:

> "**Landlords which lease land by way of a ground lease do so expecting a lower return than if they leased both land and improvements. The rent is correspondingly lower. Landowners who take the economic risk of effecting improvements to their land and then letting it out obtain a higher return in consequence.** Amongst the risk for those who effect improvements to land is that, as the improvements age and economic circumstances change, the chance increases that the improvements may become subject to increasingly onerous limitations on alteration, demolition or usage. ...
>
> What cannot be taken into account is the valuation of the improvements effected on that land and any limitations on usage of them. **What must be valued is what a prudent lessee would offer for the land as so defined excluding the improvements but subject to the terms of the lease even although ... that may bear little relation to the value of land.**" (Emphasis added.)

39. In *Feltex Ltd v JBL Consolidated Ltd*, [1998] 1 NZLR 668, 670-1 Henry J said in relation to an assessment of the fair annual rental for 5 years of an industrial property:

> "It is however necessary to keep in mind that the valuation must still be fair. The requirement of fairness means that it is not simply a matter of determining the least amount which the lessee will pay as obviously he will pay as little as he can. Rather the inquiry is as to what a prudent lessee would pay for these premises, having regard to the terms and conditions of

> the lease. This must represent the amount which he can reasonably expect to pay for the rights and obligations which are undertaken in the lease. That is **where the element of fairness lies as the lessee cannot expect to receive the benefits without payment of a fair consideration for them**." (Emphasis added)

40. The same Judge, in the same case emphasised the need to consider the terms of the lease. Of particular relevance in the case before him was the term of the lease, 30 years, and the rent review periods, 5 years. He acknowledged that a rental could well be different were the lease to be only one of a year, as against, say, 7 or 21 years. Later, in his judgment at p 672, the Judge said:

> "It is proper valuation practice, and in accordance with legal principle, when making a valuation of this nature to have regard to comparable properties. That will usually involve a comparison of many factors as between the comparable property and the subject property, and making appropriate adjustments for any distinguishing factors – and there will often be many. Included in these, **when dealing with leasehold property valuations, will be any relevant difference between the terms of two leases being compared. Only in that way can like be compared with like and overall fairness be obtained**". (Emphasis added)

41. The word 'fair' in the expression "fair annual rental" does not open up a wider inquiry as to the personal circumstances of either party. It is not a fair rent for any particular lessee to pay, but what is a fair rent for the premises. The word "fair" is insufficient to displace the hypothetical market basis mandated by the rent review clause. "Fair" tends to emphasise the disregard of comparables which are unfair. (See *Sextant*, the judgment of Richardson J.)

42. The arbitration award of the Honourable Sir Trevor Henry in *Re Te Aute Trust Board* delivered in May 1980, is helpful for present purposes. The learned arbitrator was assessing the ground rents of perpetual leases of farming properties in the Hawkes Bay held under Glasgow leases. His award is reported in the Valuers' Journal (1980) at p 801. The following quotation is highly apposite to the present case:

> "The task which I have to perform is to **place myself in the armchair of a prudent farmer** who desires to renew his lease for a further period of 21 years and to pay a fair rent. He is in possession of the land on which he is carrying on a farming business and he has, except for the Lessor's interest ascertained as earlier stated, the ownership of the improvements. In my view **the prudent lessee ought to be one who can provide sufficient capital and finance to acquire assets essential to his business and also pay a fair rent for the further asset, namely, the land which he requires for his farming business. The assets which a prudent farmer ought then be able to supply for a farming business include the land for which he must reasonably expect to pay a fair rent**. Provision for rent must take its place with all other requirements and is not to be postponed to a subordinate position so that the only capital requirement for a prudent lessee is 'sufficient

for a deposit'. In this respect I see no difference from the purchase of a freehold property except that only rent not capital is required to acquire the land." (Emphasis added)

43. The Rt Hon Sir Ronald Davison QC, in a 1992 award which fixed the rent for some Glasgow leases in downtown Auckland, made the following observations which are of general application to rent-fixing exercises of this nature (*Melanesian Mission Trust Board v Clayton Cross*). Sir Ronald's approach shows that a mechanical application of a percentage to the unimproved value is too rigid when assessing ground rent. Matters weighing with the prudent lessee must be considered also.

> **"Rental Factor Approach**
>
> This method of assessment of ground rental depends upon the determination of the two major components. First, the unimproved land value, and second the rental factor to be applied. Variations in the unimproved land values arrived at, and in the rental factor to be applied, can produce greatly differing results when calculated into the annual rental to be paid under the lease. **A simplistic or mechanical application of the rental factor formula, equating the rental factor to an interaction of interest rates, inflation rates and term of the lease, does not, in my mind necessarily, however, reflect the rental that a prudent lessee might pay in any particular case**.
>
> The rental factor is arrived at by determining a figure which over the term of the lease will return a rental commensurate with the yield of alternative forms of interest-bearing investments, such as mortgages and Government Stock, taking into account perceived trends in inflation, but making due allowance for the better security afforded by the ownership of real property. The advantages of owning land as an investment are such that the rental factor is invariably below the ruling rates of interest on other investments.
>
> While such method is commonly adopted by professional valuers as a method of assessing ground rentals, it seems to me that **if determination of the rental factor is simply the result of applying an interest rate and inflation assessment to a predetermined unimproved land value, it has built into it a certain rigidity which does not enable the valuer to take into account some of the other factors which might well weigh with a prudent lessee in making his decision**. He cannot, of course, adjust the valuation of the land, because that is normally fixed, having regard to certain standard criteria. The **only element of the computation that is available to him, in order that his decision might reflect such matters as he considers have a bearing on the rental he is prepared to pay, is the rental factor which is applied to the land value. Almost all the valuations which I have seen in the various Awards over recent years have treated the ground rental calculation virtually as a matter of rote, by taking the unimproved land value and then by applying a rental factor which is determined to a great extent by the historical trends which are reflected over the years**.
>
> **Whilst historical evidence of rental factor rates may be useful as a guide to a value in determining what the rental factor should be in a particular case, the valuer must be astute to determine whether or not there exist at the relevant date influences, conditions, or matters which would have the effect of causing a prudent lessee to assess a factor different from that arrived at on a simply mechanical basis. Or perhaps after having arrived at a rental factor in the usual way, and assessed a rental accordingly, to then adjust the rental figure arrived at, up or down, to take account of such other matters affecting rental as may be considered relevant by the prudent lessee**." (Emphasis added)

Sir Ronald, in the last paragraph above, was emphasising the need to take all matters into account and not apply a mechanical formula. This statement justifies the value in "standing back" before fixing a rate based on adjustments from alleged comparables.

LESSOR'S EVIDENCE

44. Mr Gordon acknowledged that the determination of the "fair annual rental" under the Act requires an objective determination, which has regard to the terms of the lease but not to the personal circumstances of the parties. He considered the use of comparable market lettings as the most appropriate method of valuation and eschewed other methodologies which involved the valuer making subjective judgments. Put another way, the market determines the rental not the *"artificial permutations and computations (sic) of a notional prudent lessee"*. The rental should be a percentage rate applied to the current market rental for each of the 30 indicator properties.

45. Mr Gordon saw no need to make any adjustment to the rent rate derived from the comparable market data for the land, plus the right to Fonterra shares where applicable. With regard to improvements on the land, there should be no or only minimal adjustment. Although depreciation of these improvements occurs, appreciation can likewise. Physical damage can be insured against and, nowadays, structural improvements (such as fences, water supply and race access) are at much less risk of functional obsolescence, thanks to technology.

46. A West Coast lessee has various detailed contractual obligations not to impoverish or waste the land and to keep improvements on the land in good order. He/she is required to pay rates and outgoings.

47. The valuers were able to agree on the current market rentals for the 30 indicator properties. They had evidence of open-market leasing of comparable properties. They had details of term, renewal rights, subject matter (ie bare land, land and buildings, with or without Fonterra shares, production and ebit data). 3 years was a fairly usual lease term, but longer was encountered where the lessee was to undertake some capital expenditure. Rent review intervals varied with 1, 2 or 3 year periods. A ratchet clause usually applied. Lessees met all farming expenses, rates, insurance and administrative costs. The lessor's Fonterra shares (where applicable) would be assigned to the lessee for the term of the Lease.

48. Mr Gordon saw no need to adjust the rent rate derived from comparable market data for the land plus the right to all Fonterra shares where applicable in assessing the ground rent under the subject leases. In his view, the rental paid by the prudent lessee is a holistic judgment not one reached on a piecemeal basis. Mr Gordon's figures can be seen in the appropriate columns of the summary of calculations which is annexed as Schedule 2.

49. He noted the tension between the ebit residue and the assessed market rental. The ebit is usually consumed by the rental without a return rate being applied to the lessee's livestock and other assets. He noted that farmers, in the market for a limited resource like land, will discount academic return rates for their wages and management. He considered it artificial to drive a risk-adjusted return rate onto both the lessee's return for management and assets employed so as to reduce the proportion of ebit payable for unimproved land below the proportion of ebit payable as rental for the freehold.

50. Certain leases on the West Coast of the South Island known as the *Mawhera* leases operate under the same legislation as the Taranaki leases under review. Several of these leases are used for dairying. The lessor there, in terms of the legislation, sent each lessee a notice seeking a rental for the 7 year period beginning 1 January 2001, based on 6% of the unimproved value of the land. None of the 10 lessees disputed the assessments, which therefore became the rentals payable. The notice sent out by the lessor did not refer either to the changes in rental calculation brought about by the 1997 legislation nor to the lessee's rights under that legislation to contest the assessment. A statement was put in by consent during the lessees' case from a Mr J. D. O'Connor of Westport, one of the *Mawhera* lessees. He claimed that he and other lessees had been unaware of their rights and had just accepted the assessments without challenge and without obtaining valuation or legal advice. Mr Gordon considered that, whilst not determinative for the Taranaki leases, the 6% rate for *Mawhera* leases supported his view for properties with low unimproved value. Both valuers accepted as a valuation principle that high-value properties tend to attract lower percentage rental rates and low-value properties higher rates. Mr Larmer was dismissive of the *Mawhera* rental evidence because there had been no robust assessment process, such as a discussion between two valuers or the award of an arbitrator. He suspected that the valuers concerned may have taken an incorrect approach to the valuations.

51. Because the present rent review period is for 7 years and because the statutory definition requires the fixing of a rate that is "uniform over the period", Mr Gordon adjusted the rental by adding .5% for inflation likely to be encountered over the 7-year period. Dr Stroombergen produced a graph, which showed an upward rise in Taranaki farm values over 25 years despite "bumps" both up and down. Between 1978 and 2002, prices rose at an average of .79¢ per kg of milk solids per annum, equivalent to 5.3% per annum. Escalation in land values was experienced over part of the period but they came down. Dr Stroombergen converted a 2-3 year rent (the usual market term) to a 1 year rent and then converted this to a 7 year rent. When the discount rate equalled the land inflation rate, the implied equalised annual seven year rent was .0495. Mr Gordon expressed the view that farm prices for sales after 1 January 2003 had shown an upward movement.

52. Mr Gordon saw no disadvantage to a West Coast lessee in the new statutory requirement that the lessor had right of first refusal if a lessee wished to dispose of his/her leasehold interest. Rather, he saw the requirement as advantageous to many lessees who would be able to sell without the involvement of real estate agents. He therefore made no deduction from his percentage rate to reflect a term which he did not consider disadvantageous to the lessee.

53. Mr Gordon's calculations emphasised the need to make an individual rental assessment for each property. He was critical of Mr Larmer's approach which he saw as "banding" like properties with like. Mr Gordon's percentage rental range was from 3.6% to 6% of the unimproved value of the 30 indicator properties.

54. Mr Laing is also an experienced rural valuer. In his view, the considerable evidence of lettings in Taranaki for comparable classes of land and infrastructure, made rentals from other parts of New Zealand of lesser importance. The current market rentals applied to the *Mawhera* leases could be regarded as of precedent value. He advocated an inflation adjustment. He was unhappy with Mr Larmer's approach that the hypothetical lessee would carry out the development with all the risks and uncertainties involved. The length of the development phase, in his opinion, is reflected in the assessment of unimproved value. Continuity must be preserved. He was critical of Mr Larmer's "productive" rental approach which he considered inconsistent with the purposes of the Act, particularly when compared to the agreed return for land applied to the agreed unimproved value for each property. He said in

relation to the traditional method, *"I wouldn't question that as being the most appropriate method"*.

55. Dr Stroombergen, besides dealing with the inflation adjustment, gave economic evidence to the effect that, whatever the average rate of return on the whole dairying operation, the rate on the Fonterra shares should not be higher than the rate on improvements and land. The total rent is determined in a competitive market. The witness agreed that a lessee would pay something less for a property where there was a restriction on the unreserved right to assign – such as offering first refusal to the lessor. He acknowledged differences between the situation of the notional prudent lessee of unimproved land under the perpetual lease and the actual market lessee of the land in its actual condition. For example, the latter can walk in immediately with a herd and start farming. The latter has to clear and develop the land before farming can start.

56. The witness agreed in principle that a market in land took time to slow down and then start up again. He acknowledged that predicting land values in 7-years' time was a speculative exercise in forecasting. He also appeared to acknowledge that a lease with a compulsory right of first refusal of the lessee's interest in favour of the lessor, could be a little less than one where the lessee had unrestricted right of sale.

EVIDENCE FOR THE LESSEES

57. Mr Larmer considered that the "traditional" methodology was unhelpful, given the lack of an open market for leasing unimproved land. The "classic" approach (called by him "modified classic") had to be used by comparing rental rates for other ground leasing returns and making necessary adjustments, with the aim of equating the comparables with the subject leases. One should then analyse market rentals for developed properties in an attempt to impute a rental for the unimproved land factor included in the total package acquired by the lessee of improved land.

58. A third approach, in Mr Larmer's view, was the "productive" approach which is useful where, as here, the subject properties have an agreed "highest and best use" ie dairy farming and where the valuers have agreed on productive capacity. This approach can serve as a check methodology and generally will indicate rentals that are lower in comparison with other forms of investment. Productive capability is reflected in the Rate of Return based on average farming efficiency standards.

59. Mr Larmer stressed the prudent lessee approach, as established by authority and also the proposition that valuers should consider all methodologies appropriate in the circumstances. He noted the dictum of Smith J in *Wilson* (*cit. supra*) that *"rent is fixed by an expression of an informed judgment on all relevant factors"*. Also, the approach in the *National Bank* case (*cit. supra*) that Courts *"... are unwilling to be drawn into giving a direction that the valuation must be made by adopting one particular method"*.

60. He concluded that, given the economic and industry conditions prevailing at 1 January 2003, the prudent lessee would pay more attention to farm business fundamentals than would have been the case in the highly inflationary environment prevailing when the 1980 Te Aute rentals were fixed by Sir Trevor Henry. The high level of values at the present review date, despite a downturn in revenues, means that the prudent lessee must pay particular attention to what the "fair annual rent" represents as a cost of using the capital represented by the unimproved value assessment.

61. His extension of the "classic" approach involved a consideration of developed properties in the area. There is not a "like for like" comparison but the subjective imputing of rates to various components of a developed property.

62. Mr Larmer produced a review of rural rental awards in long-term perpetual leases over a wide geographical spread and over a range of different land issues. He acknowledged that no "greenfields" lettings were revealed and that rent reviews either negotiated or arbitrated are not considered to be as helpful as "greenfields" lettings. He was dismissive of using the *Mawhera* rentals as a guide, characterising them as passive acceptance by lessees through ignorance and default without any lessees' organisation, any professional advice and with a non-rigorous valuation approach by the lessor's valuer.

63. Numerous problems stand in the valuer's way in making comparisons with other rent fixings meaningful to the present exercise. The "comparables" bristle with differences of terms, lease conditions, locality, economic use, land type, etc. The most the valuer can do - what Mr Larmer claims to have done - is to make a series of subjective adjustments so as to achieve a degree of compatibility.

64. The Rent Reviews and Awards considered by Mr Larmer are now summarised. All but two were undertaken by registered valuers acting either as arbitrators or umpires.

(a) **Ngati Rarua Atiawa – 1995 – Motueka**

This involved 8.2 hectares of high-value horticultural land held under a 21-year perpetually renewable lease with 10.5-year rent reviews. A previous award by an umpire 10.5 years previously (Mr PGS Penlington QC) had been made at a time of high inflation. The 1995 arbitrator noted evidence of reduced inflation and interest rates since the previous award. Consequently, the earlier award could not have reflected these changes. In fact, rental yields on rural property had dropped. He fixed the rate for the renewal at 5%, as distinct from the lessor's contention of 6.04% and the lessee's of 4.65%.

(b) **Taranaki Endowment Trusts – Review**

These perpetual leases, required rentals for 21 years to be fixed as at 31 December 1995. Unimproved values had been agreed upon by the valuers. The arbitrator held that the rental percentage should vary between 3.38% and 4.37% because of the differences in unimproved state of the subject properties. Mr Larmer considered that this land, although in Taranaki, was not typical of West Coast lease land. Rentals were fixed for 21 years. Further Endowment land in Taranaki came up for review in 1997 with similar results (ie around 4%).

(c) **Whitford**

This award, published in December 1999, related to a 21-year perpetual lease of land at Whitford near Auckland with soils of low productivity but with "lifestyle" potential as well as farming use. The rate fixed by award was 2.44% based on the average of the unimproved values put in evidence.

(d) **Waerenga-a-hika: Rent Review**

This award was concerned with high-quality Poverty Bay cropping land. The learned umpire (Mr M.D. Chrisp, a well-known Gisborne solicitor) had to fix rent for a 7-year term under a perpetual lease. The umpire considered that rental fixings outside of Poverty Bay were of little help, given the region's isolation. Another point of difference was that the ground rent had to be set on modified land value plus the value of certain lessor improvements. Mr Chrisp preferred the land use approach and adopted a 3% rental increased by .7% for inflation. It is interesting to note in this Award, as with the *Clayton Cross* case (*supra*), that the arbitrator considered that evidence of

short-term lettings would be a factor influencing the notional prudent lessee provided *"adequate and sound adjustments can be made to differentiate between those leases and the type of perpetual lease with which we are now dealing"*.

(e) **Wakatu Award**

In 1999, an arbitrator fixed at 5% the 21-year rental rate on a perpetual lease of horticultural land near Motueka. Rental evidence was unsatisfactory as being marginally comparable.

(f) **Te Aute Consent Awards**

This was the next 21-year review after Sir Trevor Henry's 1980 award. In early 2001, a ground rent rate for 20 properties was set by consent at 5.5% reduced by .75% for lifestyle blocks.

65. Mr Larmer then adjusted these awards for direct comparison with the situation for the West Coast leases as at 1 January 2003. The adjustments were for:

(a) **Time**: (most were 21 years, some 7);

(b) **Date**: 1995-2000 were, in Mr Larmer's view, superior years for pastoral farm economies than 2002. Although dairy improved from 1995/6, conditions in horticulture were difficult. Beef, sheep meat and wool improved in recent years with the lowering value of the NZ dollar. He explained his reasons for his adjustments. For example, he adjusted the *Mawhera* rents down to 5% because of the buoyant 2000/1 period for the Westland Dairy Co Ltd (not part of Fonterra). All the *Mawhera* leases fell due on 1 January 2001 and not 1 January 2003.

(c) **Terms and Conditions of Leases**: Mr Larmer made a slight deduction because of the allegedly onerous right of first refusal which the lessor gained from the 1997 legislation. This right had not been imposed on the lessees in the examples of other rent-fixings.

66. Mr Larmer made no allowance for inflation over the 7-year rent period, despite the requirement in the statute for a "uniform" fair rate over the whole of the period. He

considered that farm values had peaked and would recede. However, like a locomotive, it takes a long time for land values to stop and then reverse. He did not see any likely increase in the unimproved value over the 7-year period. He instanced 7 year periods in the past where there had been no significant increase in value.

67. Mr Larmer produced a table showing his adjustments for the 50 odd widely dispersed "comparables". He disregarded those at either end of the range as "outliers". His table, as given in evidence, was:

Year	Party/Location	Agreed or Decided Rent Rate	Adjust for Term	Adjust for Date	Adjust for Lease Provisions	Rent Rate Equiv Jan 03
1995	Ngati Rarua/Motueka	5.00	-	-	0.25	4.75
1995-97	Taranaki Endowment Leases/Whenukura	4.00	-	0.30	0.20	3.50
1998	St Stephens and Qvict/Whitford	2.44	-	-	0.15	Say 2.30
1999	Waerenga-a-hiki/Proverty Bay	3.06	-	-	0.15	Say 2.90
1999	Wakatu/Motueka	5.00	0.25	-	-	4.75
2000	Te Aute Small Rural Holdings/Hawkes Bay	4.75	0.50	0.50	0.25	3.50
2000	Te Aute Farm Properties/Hawkes Bay	5.50	0.55	0.75	0.30	3.90
2001	Mawhera/West coast, South Island	6.00	-	1.00	-	5.00

He considered that the table "pointed to" a rental rate factor of under 3% for high value land and up to 4% for low value land.

68. In cross-examination, Mr Larmer accepted that he had given insufficient weight to the top end of the range. The conclusions following from this concession resulted in a lift in his range of rates from 3% to 4.25%.

69. Mr Larmer, unlike Mr Gordon, but like Sir Ronald Davison and Mr Chrisp, did not see market rentals for farms of improved land as being true comparable to rents paid by the notional lessee of unimproved land under a perpetually-renewable lease unless there were adjustments. He extracted the market rental as a percentage of the market value in each case with a range from 3.75% to 6%, with a two-thirds around the 4-5% range.

70. He adopted a "top down" approach to imputing a return to unimproved land. It is not enough to exclude improvements. Their physical existence has to be set aside in terms of the statute.

71. Mr Larmer strongly rejected unadjusted market rentals as a guide for fixing the ground rent under a West Coast lease. He listed several points of difference. The principle ones are:

(a) The short-term tenant can "walk on" to the land and begin farming operations immediately whereas, the notional prudent lessee has to develop the land – a process which for some of the properties, originally heavily-bushed, could take more than the 7-year rental period.

(b) The short-term tenant has a term of 1, 2 or 3 years with possibly frequent rent reviews and a ratchet clause. The notional prudent lessee is locked into a perpetual lease relationship with the lessor.

(c) The short-term tenant can have little or no capital input, whereas the notional prudent lessee has to spend capital sums to bring the improved land into production.

(d) The rent-fixing process for the short-term lease is usually easier and cheaper than for a perpetually-renewable lease at 7 yearly intervals.

(e) Various factors can influence the parties in entering into a short-term lease which are not found in the perpetually-renewable lease relationship. The lessee for the short-term may wish to supplement an existing farm or to provide land for a family member or sharemilker to develop his/her own farm. A short-term lessor can demand a higher rent than may otherwise be justified, which the tenant may be willing to pay for all sorts of non-market-related reasons. Unlike the short-term lessor who can adopt a "take it or leave it" attitude to the lessee, the hypothetical prudent lessor under a perpetual lease must accept whatever rental it is appropriate for the prudent lessee to offer.

72. Mr Larmer instanced as reasons for a tenant agreeing to pay a high short-term rental:

(a) synergies or economies of scale with existing land;

(b) a wish to build up Fonterra shareholding;

(c) a means of increasing stock numbers;

(d) an opportunity to improve the career path for family and others.

73. He acknowledged the anomaly that the likely ebit would be extinguished by the market rent. This pointed to a need to looking at the productive or economic approach. A prudent lessee is entitled to look back, in order to judge future conditions. Hence, Mr Larmer's use of the productive approach as a check on the traditional and classic methods.

74. Mr Crighton advised Mr Larmer, when the latter analysed developed market rentals back to the "fair annual rent", Mr Crighton's view was that the return rate to development and shares is usually higher than the derived market rental rates. This resulted in the "modified classic" methodology which Mr Larmer acknowledged could not be regarded as a primary approach. It does compare "like with like", although with much subjectivity.

75. Mr Larmer's view was that the statutory requirement that the lessor has a right of first refusal to any of the leased properties justified a differentiation of .25% when compared with perpetual leases which do not have such a requirement. He also pointed out that whilst there, is on paper, a right to a lessee to freehold, that right is effectively nugatory. Even if the lessor wished to sell the freehold (which does not appear likely under its current policy), it would be obliged to offer the land to Maori interests in accordance with current legislation. He referred to the difficulties encountered when one of 3 brothers who had farmed 3 separate leasehold properties as one farm, wished to exit the partnership and to sell to his brothers the one discrete leasehold block held in his name. Instead of being able to transfer the block to his brothers as part of an agreed restructuring, the block had to be auctioned because of the "buy-back" requirement in favour of the lessor.

76. As noted in paragraph 66, Mr Larmer made no adjustment for inflation (or "mid-term rental formula" as it is called sometimes). Any adjustment upward was unjustified by the conditions faced in the dairy industry. There is no current rampant inflation, as was the case when the Te Aute rents were fixed in 1979/80. The term of 7 years is only slightly more than twice the term of the standard 3 year lease. He concluded that there was likely to be the same scenario for the period 2001-2008 as in the

period 1993-2000 when land values drifted backwards from the 1993 peak levels until an upward movement in 2000. A similar situation took place in the period 1983-90. Because the process of agreeing ebits with Mr Gordon looked towards returns in the future, any upward adjustment was see as "double dipping".

77. Very conservative return rates were imputed by Mr Crighton and Mr Larmer to improvements and Fonterra shares, in an attempt to replicate the rural land market expectations of return excluding capital gain. The lack of empirical data for returns to the components of a rented improved property results in significant analysis limitation. Mr Larmer's calculations (as seen in the Table published as Schedule 2 to this Award) give a "fair annual rent" for each property assessed on market rent comparisons in the undeveloped state analysed back to a residual surplus. Some rents gave a much greater return on unimproved land than is achievable by a normally efficient farming operation. Mr Larmer's range of rates is from 3.25% to 3.75% with many properties at the 3.75% range.

78. The various calculations of the valuers for each of the 30 properties are reproduced in Schedule 2. The first 5 columns of figures show the agreed data. The next show i) the market rent expressed as a percentage rate of the agreed unimproved value which is the same as Mr Gordon's percentage for the "fair annual rent", ii) Mr Larmer's results by the 3 modes of assessment on which he relied, (iii) Mr Gordon's and Mr Larmer's differing assessments of the "fair market rent". In Mr Gordon's case, he has simply used the same percentage for the rent of the notional unimproved property as is revealed by the rent of each property in its current developed state plus a .5% add-on for inflation. Mr Larmer claimed to have formed a judgment, in each case, based on the results from the three methodologies and based on adjustments for consistency. He claimed that it was the valuer's duty to "stand back" before making a judgment and not to apply a percentage to unimproved value in a mechanical way. He also deducted .25% for the perceived disadvantage to the prudent lessee inherent in the statutory term of the lease which requires first refusal to the lessor.

79. Mr Crighton assessed the appropriate return on capital to allow for the non-land assets of the farm business and the relevant economic concepts. Having regard to the recognition by farmers of low returns, excluding any capital gain, he imputed low rates of return to these assets. The lessee under a perpetual lease has to consider his/her ebit as being a bundled return on assets owned and the asset leased (the

land). Under this approach, higher residuals accrue to the unimproved land than would otherwise be the case.

80. Mr Crighton has both valuation and accountancy qualifications. He emphasised the "prudent lessee" approach as the major driver of the perpetual lease rent assessment process. He considered that the prudent lessee would look at a range of factors, including the productive capacity of the land in its unimproved state, the farm surplus available from which the rental could be paid, the risks and returns associated with the various capital improvements of the business alternatives, including leasing fully-developed properties and market leasing evidence.

81. Whilst acknowledging the "traditional" approach, this witness adopted the "productive" approach based on what he saw as basic economic principles. He concluded that there was a need to distinguish between a rental for a developed property and a rental for an unimproved land where the lessee owns the improvements. The lessor of the developed property owns a portfolio of assets and the rental received represents a weighted average return on all parts of the portfolio. He accepted as correct the differences seen by Mr Larmer between a market lease of a developed property and a perpetual lease of bare land. He felt that "fair annual rent" cannot be determined without reference to the ebits. This is consistent with economic theory and the prudent lessee test.

82. Dr Anderson considered, from an economist's standpoint, how an appropriate rate of return for the lessor on unimproved land might be determined from an investment point of view. He considered that the only reason that current lessees can afford to rent the land at present is because the development has been done. They are earning a return on an improvements value lower than the level of investment needed to reinstate those improvements. This factor effectively provides a residual return to the assessed unimproved land.

83. This witness also concluded that an unadjusted application of the "traditional" approach to rent assessment would lead to inconsistent outcomes. The process is severely contained by the inherent uncertainty surrounding unimproved land values. After consideration of evidence from the forestry and commercial property markets, Dr Anderson supported Mr Crighton's conclusion that the implied rental yield on the value of the unimproved land (the lessor's asset) is lower than the rental yield on the total value of the assets used in the farming operation (the lessee's assets).

DECISION ON RENTALS

84. The authorities are clear that the Arbitral Tribunal – which is effectively acting as did an umpire under former rent-arbitration regimes – is not required to follow any particular principle of valuation. The Arbitral Tribunal, having considered the evidence and submissions must reach an informed judgment that is just and reasonable and based on the authorities. As counselled by the *Clayton Cross* case, there should not be a mere mechanical application of a rate to the unimproved value.

Market Rental Approach

85. The Arbitral Tribunal does not favour the method favoured by Mr Gordon, which was based on the unadjusted agreed market rental for each property in a developed state. That cannot possibly provide a true yardstick for fixing rentals for land in the hypothetically-undeveloped state. The differences are obvious. The principal one is that the market lessee of developed land can walk in with his/her herd and start farming right away. On the other hand, the hypothetical prudent lessee of the hypothetical undeveloped land has to undertake the task of development of the bare land. That task could take up to 8 years for some of the properties which are presumed to be in their pristine state.

86. Secondly, the situations of the lessor of the improved property and the lessor of the perpetually-leased property are starkly different. The former can assume a "take-it-or-leave-it" attitude to a prospective lessee who may be prepared to pay a very high rental for extraneous reasons, such as those mentioned by Mr Larmer. The latter is locked into the perpetual lease and is, at law, entitled to receive only what it is reasonable for the hypothetical prudent lessee to offer. Moreover, the hypothetical prudent lessee knows that he/she has perpetual rights of renewal as well as a very marketable asset – albeit subject to the lessor's right of first refusal.

87. Sir Ronald Davison in the *Clayton Cross* award and Mr Chrisp in the *Waerenga-a-Hika* award saw the need to make adjustments to market rentals for developed land before using them as guides to ground-rent fixing. Mr Gordon submitted that the market sets the rules, but with respect to him, there are two different markets. One market is for the leasing of improved land in Taranaki today and the other is peopled by the unreal and shadowy personae of the hypothetical prudent lessee and lessor who are considering the rental for land in its undeveloped state. In *Granadilla*, it was submitted that the umpire was wrong not to have placed much weight on evidence

about market rentals for sites other than those held under perpetually-renewable leases. The umpire took the view that, for such evidence to be relevant, it must be of comparable, new, open-market, perpetually-renewable leases. The Court upheld Goddard J who had said that the umpire had found the market evidence *"... of limited use because it was neither directly nor truly comparable. That finding was open to the umpire on the evidence which minimised the usefulness for comparative purposes"*.

88. There are other differences between the two types of lettings that were canvassed in submissions and in evidence. The above are the major ones but the others such as lack of development land, optimistic assessments of the market, short-term leasing to obtain more Fonterra shares all tend to show that the unimproved value of a developed leasehold dairy farm is not necessarily a pivotal issue in the short-term lease of that farm.

89. Counsel for the lessor submitted that market rents – not the unimproved value – set the correct relativity amongst the 30 indicator properties. The basis of this submission was that the unimproved values are a residual, often starting with the capital value, which includes what Dr Stroombergen described as "consumption returns" (ie value for reasons other than productivity). Capital value would also have deducted from it the added value of existing improvements which might be redundant to creating productivity (eg a second house) or reflect other than the land's highest and best use (eg horse stables).

90. This submission stressed that Mr Larmer's approach postulated only three different rates which disturbed relativities. He had only three bands, whereas there should have been at least 5. The Arbitral Tribunal does not consider banding *per se* to be necessarily objectionable. Many properties in the 30 have similarities on several counts and it would be surprising if the range of percentage rentals were broad.

91. This submission of the lessor's does not enhance the acceptability of the comparative market rental as the appropriate methodology. However, it does emphasise the need, when making the final assessments, of paying close attention to relativity. To have two adjacent farms each with a comparable state of development, paying divergent rental rates, would not be fair.

92. The Arbitral Tribunal does not disregard the market rental evidence. However, it must be used as a guide only, bearing in mind the differences between market rental

of an improved property and ground rental for an unimproved property. If nothing else, the market rental provides a rate beyond which a ground rental cannot go (at least before the imposition of any "mid-term" adjustment).

TRADITIONAL/CLASSIC APPROACHES

93. Drawbacks exist in relying too heavily on rentals for other perpetual leases to provide indications of comparable rentals. Mr Larmer made adjustments and acknowledged many of the deficiencies in the precedents. However, he was unable to find any more helpful transactions. The following comments can be made.

(a) Generally, there are very few points of similarity. All except the Taranaki Endowment leases are out of district. None, apart from some *Mawhera*, are for dairy farms. Many are for 21 year rentals. Some are as old as 1995.

(b) The Arbitral Tribunal is of the view that the Whitford rental is so far removed from a Taranaki West Coast lease that it is of no help at all in the present exercise.

(c) The Arbitral Tribunal cannot dismiss the *Mawhera* rent-fixing process quite as readily as does Mr Larmer. It is a big ask to assume that 10 different lessees were all so confused about their rights that they passively accepted their lessor's assessment. Most lessees who challenge the rental claims of lessors do so without the benefit of an association of lessees which is hardly a point of distinction. Mr O'Connor's statement must be regarded as an exercise in hindsight. *Mawhera* must be regarded as a comparable since the leases were identical in terms. Because the *Mawhera* leases, generally speaking, had a low unimproved value and were fixed 2 years ago, the precedent is more useful for the lower end of the 30-property spectrum.

94. The comparables (apart from *Mawhera*) are so inherently unhelpful that the approach of Mr Chrisp, the umpire for the *Waeranga-a-hika* rental is tempting. He refused to accept the out-of-district comparables because of Poverty Bay's isolation. Nevertheless, the Arbitral Tribunal pays some heed to Mr Larmer's adjustments, given his huge experience, but makes the reservations made in the preceding paragraph. In the end, his calculations are part of the collage of information and methodology which the Arbitral Tribunal must utilise in making decisions on the individual rentals.

95. Counsel for the lessor made several detailed criticisms of Mr Larmer's adjustments as shown in para 67 above. He pointed out, correctly, that the Taranaki Endowment settlements were at 4 rates, 4.25%, 4.4%, 3.38% and 4.37%. This gives an average of 4.1%, so Mr Larmer's 4% is not really flawed. Further, if Mr Larmer's traditional approach is to have any validity, after excluding the highest and lowest and accepting his adjustments, the result must give a range from 2.9% to 4.75%. Any subjective analysis must come after the bands have been established. In other words, the subjective judgment can be exercised only once – after the band of rates has been established.

96. Counsel for the lessor also criticised details of Mr Larmer's subjective adjustments for date such as .75 for Te Aute 2000, .30 for Taranaki Endowment and 1% for *Mawhera*. He then adjusted for economic outlook under the heading "Term" because these rentals were set at the beginning of the 2000/2, land "spike". Wakatu .25, Te Aute Small Holdings .5 and Te Aute Farms .55 were characterised as "double dipping" because these were adjustments for a different economic situation from that facing the Arbitral Tribunal in Taranaki 2003. The combined assessment, according to counsel, is "back to front" because the major adjustments are for the most recent settlement which would have been at the time of the same upward land trend.

97. Counsel for the lessees, in defence of Mr Larmer's approach, acknowledged the care needed in making the adjustments of the "comparables". The relevance of the traditional method is that the unimproved value of the land has been established and that, whatever its use, that is the value prescribed in the hypothetical leasing situation. Counsel referred to various tables produced by Mr Larmer which showed how he had addressed relativity and consistency founded on a direct comparison approach to market rents. In the following table, the rate of return on total farm capital is a cross-check.

Value Band $ (per ha)	Property No.	Name	Fair Annual Rent	UV per ha	Rent per ha	Rental Rate	Est ROR Total Farm Capital
10-10,000	3	Watson	14,065	1,490	56	3.75	3.05
	5	Emeny	11,625	3,350	126	3.75	4.70
	7	Haigh	6,190	3,580	134	3.75	4.20
	27	Forman	14,250	3,725	140	3.75	4.20
	24	Death	8,250	3,740	140	3.75	4.45
	25	Wallace	12,000	4,010	150	3.75	4.45
	30	Whatalotta	43,500	4,560	171	3.75	4.20
	11	Armstrong	9,565	4,740	178	3.75	4.80
	12	Armstrong	10,875	4,835	182	3.75	5.45
	13	Armstrong	11,065	4,860	182	3.75	5.00
	14	Armstrong	21,000	4,855	182	3.75	5.25
	23	Thompson	7,500	4,880	183	3.75	4.45
	9	Christie	16,315	5,700	214	3.75	4.10
	10	Hickey	18,190	5,980	224	3.75	4.10
	22	Cook	12,750	6,665	250	3.75	3.70
	28	L Williams	48,750	8,440	317	3.75	3.90
	8	Tioko	14,250	9,100	341	3.75	4.90
	29	Kohi (Dickie)	16,875	9,265	347	3.75	4.35
10,000-20,000	20	Wrigley	14,700	11,630	407	3.50	3.60
	16	Palfrey	26,075	11,975	419	3.50	3.85
	2	MacKenzie	33,775	12,900	452	3.50	3.95
	6	A Williams	31,500	11,975	480	3.50	3.70
	17	Sayer	19,950	13,735	480	3.50	3.75
	15	Brophy	29,400	13,790	483	3.50	3.70
	26	Moerangi	26,600	13,895	486	3.50	3.80
	18	Van Der Fits	33,950	14,180	496	3.50	3.70
	1	Guthrie	16,100	14,465	506	3.50	3.55
	4	Bolton	13,300	19,000	663	3.50	2.50
	21	Walsh	10,075	20,665	669	3.25	3.20
	19	Sanderson	7,960	23,330	757	3.25	3.60

98. Mr Larmer considered that the overall rate of return dictates a cap on rent rates. 3 only of the 30 indicator properties have fair annual rents as assessed by Mr Larmer that exceed the Rate of Return. 2 out of the 3 properties are not being used for dairying.

99. The table shown above shows rental rates, lower for high-value land and higher for low-value land, a principle agreed by the valuers. Relating fair annual rent per hectare to unimproved value demonstrates parcel-by-parcel relativity. Mr Larmer has valued rental per hectare for different parcels thus:

Value $1,500 per ha:	Rent $55-6 per ha
Value $6000 per ha:	Rent $225 per ha
Value $12,000 per ha:	Rent $420 per ha
Value $23,000 per ha:	Rent $750 per ha

100. In support of Mr Larmer's views, Counsel for the lessees claimed that Mr Gordon's approach of having regard only to market lettings of improved land produced erratic results. For example, on land around $3,500 - $3,750 per hectare value, Mr Gordon goes from 4.6% (Property 3) to 6% (Property 24). At a slightly higher value, at $4000 per ha for Properties 23, 25 and 30, it is around 5 – 5.5%.

101. There is, according to counsel, further inconsistency when one moves into the higher $10 – 20,000 per hectare bracket. In particular, Properties 1 and 2 which the Arbitral Tribunal inspected. Both are at Tikorangi and are fairly indistinguishable – at least to the uninformed eye. Mr Gordon assessed Property 1 at 4.25% (for an area of 31.8 ha) and Property 2 (for an ~~acre~~ area of 74.8 ha) at 4.95% or $561 per hectare versus $484 per hectare. Counsel pointed out that .7 of a percentage difference meant $5,759 extra annual rent for the farmer of Property 2 more than what the farmer of the similar and adjacent farm would pay.

102. For Property 4 at Bell Block close to the city, which the Arbitral Tribunal also inspected, Mr Gordon's market rental for non-dairying was 4.8% of unimproved value which is inconsistent with his assessment for Property 1 which is quite near to Property 4.

103. Counsel for the lessees submitted, in summary, that the above examples showed anomalies in Mr Gordon's approach which should have had applied to them Mr Larmer's techniques of consistency and "standing back". In counsel's submission, it defies logic that land essentially of the same character should have widely different rental rates.

104. As noted earlier, the market rent would extinguish the ebit in most cases. This shows how unhelpful the market rental approach can be, given that the "prudent lessee" must, as Sir Trevor Henry pointed out, have the money with which to fund improvements and pay a fair price for the use of the land. Hence, Mr Larmer's productive approach is not central to his evidence but purely acts as a check. The efficacy of the productive method rather diminished during the hearing and the Arbitral Tribunal finds it of relatively minor assistance, other than as a check.

105. The Arbitral Tribunal considers that it is driven to apply the traditional approach and so has put himself in the armchair of the prudent lessee to determine what percentage of the lessor's unimproved value of the land may fairly be offered for the next 7 years of each perpetual lease on its conditions as modified by the 1997 Act, so as to reflect a uniform rate for the whole of the period. The Arbitral Tribunal broadly accepts Mr Larmer's views but has made such changes as seem appropriate. As Sir Ronald Davison remarked when making his decision as to an appropriate rental percentage in *Clayton Cross*, *"valuation is not by any means an exact science but a judgment on all information at present available"*. The Arbitral Tribunal's approach is similar to the task in hand.

106. In fixing a percentage on the above basis (before any "mid-term allowance or allowance for the allegedly onerous first-offer to lessor provision), the following matters have been taken into account by the Arbitral Tribunal:

(a) The evidence, such as it was, of rent fixing in other districts at varying dates and for leases with different rental terms and for different land uses.

(b) The *Mawhera* rent settings, 2 years ago, for leases of farms with identical lease terms but in another district.

(c) The market rental for each parcel of land in an improved state.

(d) The economics of dairy farming and of the particular properties as given in evidence.

(e) The legal requirement that the notional prudent lessee would have the financial resources both to develop the land and to offer to pay a fair rent to the lessor for the use of the land.

(f) The dossier of information about each of the 30 indicator properties which is useful for the purposes of maintaining consistency of approach for similarly-valued properties.

(g) The knowledge that the notional prudent lessee is not one to be held to ransom by an avaricious or unwilling lessor nor one unwilling to lease at a fair price for whatever reason. Rather, the notional lessor is willing to accept what it is fair for the lessee to offer in the circumstances.

(h) The whole of the evidence and the submissions of counsel, including their criticisms of the valuers and economists found in the submissions and on cross-examination.

MID-TERM RENT ADJUSTMENT

107. Counsel for the lessees submitted that there should be no adjustment for inflation, called "mid-term adjustment": he said that any justification for such an increase is pure guesswork, not borne out by the evidence. Land prices dropped in 1995-8/2000. The locomotive of price escalation needs time to slow down and stop before there can be another increase. Counsel for the lessor submitted, based on Mr Gordon's view that the market has firmed since 1 January 2003, that Mr Larmer's price "spike" had yet to occur. The two valuers had agreed on an average dairy payout for the next 7 years of $4.25. The present payout is $3.80. Dr Stroombergen's 25-year graph shows a consistent trend. Mr Larmer spoke of two 7-year periods in recent times where there had been little growth in land values. He saw the next 7 years as similar.

108. It is notoriously difficult to predict inflation. Such a task is always undertaken by an Arbitral Tribunal when assessing ground rents for a 21-year period. In the experience of this Arbitral Tribunal, in those cases there is usually economic evidence predicting inflation rates based on various indices. The soothsaying

exercise required of an Arbitral Tribunal is exacerbated in its difficulty on a 7 year rent fixing. At least with a 21-year term, one can say with confidence that there will be some unquantifiable inflation, although the extent is always arguable. The question is always whether the prudent lessee for a 7-year term would take inflation into account at all in deciding on how much to offer the lessor. The notional prudent lessee has the security of knowing that there will be no demand for additional rent for another 7 years and that he/she has a perpetually renewable tenure. These matters were adverted to by Henry J in the *Feltex* case (*supra*). That security would predispose the prudent lessee to consider factoring in a modicum of inflationary adjustment into the fair rent he would offer to the lessor.

109. The Arbitral Tribunal considers that a 7-year term is of such length as to make it more probable than not that there will be some modest increase in land values. Balancing the evidence, a .25% allowance seems appropriate.

ALLOWANCE FOR LESSOR BUY-BACK PROVISIONS

110. In summary, a lessee wishing to dispose of his/her interest in a West Coast lease must first offer the lease to the lessor. The Lessor has 20 working days within which either to accept the lessee's offer direct to it or advise the lessee whether it is prepared to better any conditional offer that the lessee may have received.

111. The Arbitral Tribunal does not consider that the provision for having to make first offer to the lessor is necessarily all bad news for the lessee. It enables a buyer to dispense with a real estate agent (although Mr Larmer said many Taranaki farm transactions do not have agents involved). The lessor may have resort to some Government funding with which to make any purchase, so that the lessee knows there is some prospect of the offer being considered if not accepted. If someone else is prepared to pay more than the lessor is prepared to offer, then, after the mandatory waiting period, that sale can proceed. The lessor's rights are not a clog on the lessee's rights, rather a hiccup (to mix a metaphor). Lessees received once only solatium and compensation payments for this change to the lease contract. All in all, the benefits to lessee and lessor are fairly evenly-balanced by this provision. The Arbitral Tribunal therefore makes no allowance for this term of the lease. The Arbitral Tribunal does not consider that consideration of any possible its onerous effects would be high on the list of considerations motivating the notional prudent lessee who would, of course, factor in possible benefits from the provision. The unfortunate example given by Mr Larmer cannot be a frequent occurrence.

112. Accordingly, the following determinations of rental are made. They incorporate .25 addition for mid-term adjustment. In the end, the Arbitral Tribunal must make what is essentially a "jury" determination based on the collage of methodologies found in the evidence. The determination also benefits from the "standing back" exercise to secure relativity, so far as is possible, in such an imprecise and artificial process.

113. The percentage rental determinations on the bases articulated in the preceding paragraphs are as follows:

Number	Name of Lessee	Agreed Unimproved Value	Unimproved Value per Hectare	Fair Annual Rent Percentage	Annual Rental for 7 years from 1 Jan 2003
1	Guthrie	460,000	14,465	3.85	17.710
2	MacKenzie	965,000	12,900	3.85	37,152
3	Watson	375,000	1,490	4.2	15,750
4	Bolton	380,000	19,000	3.8	14,440
5	Emery	310,000	3,350	4.2	13,020
6	Williams	900,000	13,720	3.85	34,650
7	Haigh	165,000	3,580	4.2	6,930
8	Tioko	380,000	9,100	4.0	15,200
9	Christie	435,000	5,700	4.1	17,835
10	Hickey	485,000	5,980	4.1	19,885
11	Armstrong	255,000	4,740	4.2	10,710
12	Armstrong	290,000	4,835	4.2	12,180
13	Armstrong	295,000	4,860	4.2	12,390
14	Armstrong	560,000	4,855	4.2	23,520
15	Brophy	840,000	13,790	3.9	32,760
16	Palfrey	745,000	11,975	3.95	29,427
17	Sayer	570,000	13,735	3.85	21,945
18	Van der Fits	970,000	14.180	3.85	37,345
19	Sanderson	245,000	23,330	3.75	9,187
20	Wrigley	420,000	11,630	3.95	16,590
21	Walsh	310,000	20,665	3.75	11,625
22	Cook	340.000	6,665	4.0	13,600
23	Thompson	200,000	4,880	4.2	8,400
24	Death	220,000	3,740	4.2	9,240
25	Wallace	320,000	4,010	4.2	13,440
26	Williams (Moerangi)	760,000	13,895	3.85	29,260
27	Forman	380,000	3,725	4.2	15,960
28	Williams	1.3 million	8,440	4.1	53,300
29	Dickie	450,000	9,265	4.0	18,000
30	Whatalotta Heifers	1.16 million	4,560	4.2	48720

114. The Arbitral Tribunal therefore fixes the rentals payable on each of the 30 indicator properties for the 7-year period commencing 1 January 2003 as stated in para 113 above. The amounts fixed are exclusive of GST. Counsel should advise if there are any calculation errors which can be remedied under Article 33 of the First Schedule to the Arbitration Act.

115. The Arbitration Agreement provides that each party shall bear its own costs. The costs of the hearing (room hire, refreshments, stenographer's fees, etc) are to be shared equally by the parties.

116. The fees and disbursements of the Arbitral Tribunal are to be borne equally by the parties.

Dated this day of June 2003

Hon Sir Ian Barker QC
Sole Arbitrator

Seat of Arbitration: New Plymouth

Schedules:
1. List of 30 lessees, parties to the Arbitration Agreement
2. Summary of Valuers' Contentions

SCHEDULE 1

Property No.	Location	Name of Lessee
1	Inland Road	Guthrie PR & S
2	State Highway 3	MacKenzie J A & M D
3	Otaroao Rd	Watson W & L
4	Devon Road	Bolton W & C
5	Kirihau Road	Emeny H & F
6	Puniho Road	Williams A & K
7	Kahui Road	Haigh D W & D E
8	Turu Road	Tioko M Estate
9	Kina Road	Christie C & P
10	Namu Road	Hickey A & A
11	Waiteika Road	Armstrong I D & J A
12	Waiteika Road	Armstrong I D & J A
13	Waiteika Road	Armstrong I D & J A
14	Waiteika Road	Armstrong I D & J A
15	South Road	Brophy J M Estate
16	Skeet Road	Palfrey L Estate
17	Taikatu Road	A M Sayer
18	Winks Road	Van Der Fits R & J
19	Rama Road	Mrs E G Sanderson
20	Hastings Road	Wrigley G S
21	Tempsky Road	Walsh P
22	State Highway 3	Cook N & B
23	Mountain Road	Thompson W & K
24	Ngawhini Road	Death J R & J E
25	Ngawhini Road	Wallace N J & M S
26	Ohangai Road	Williams L
27	Ingahape Road	Forman G
28	Otauto Road	Williams L/J Newland
29	Kokako Road	Dickie J (Kohi Meats)
30	Beach Road	Whatalotta Heifers Ltd