NEW ZEALAND

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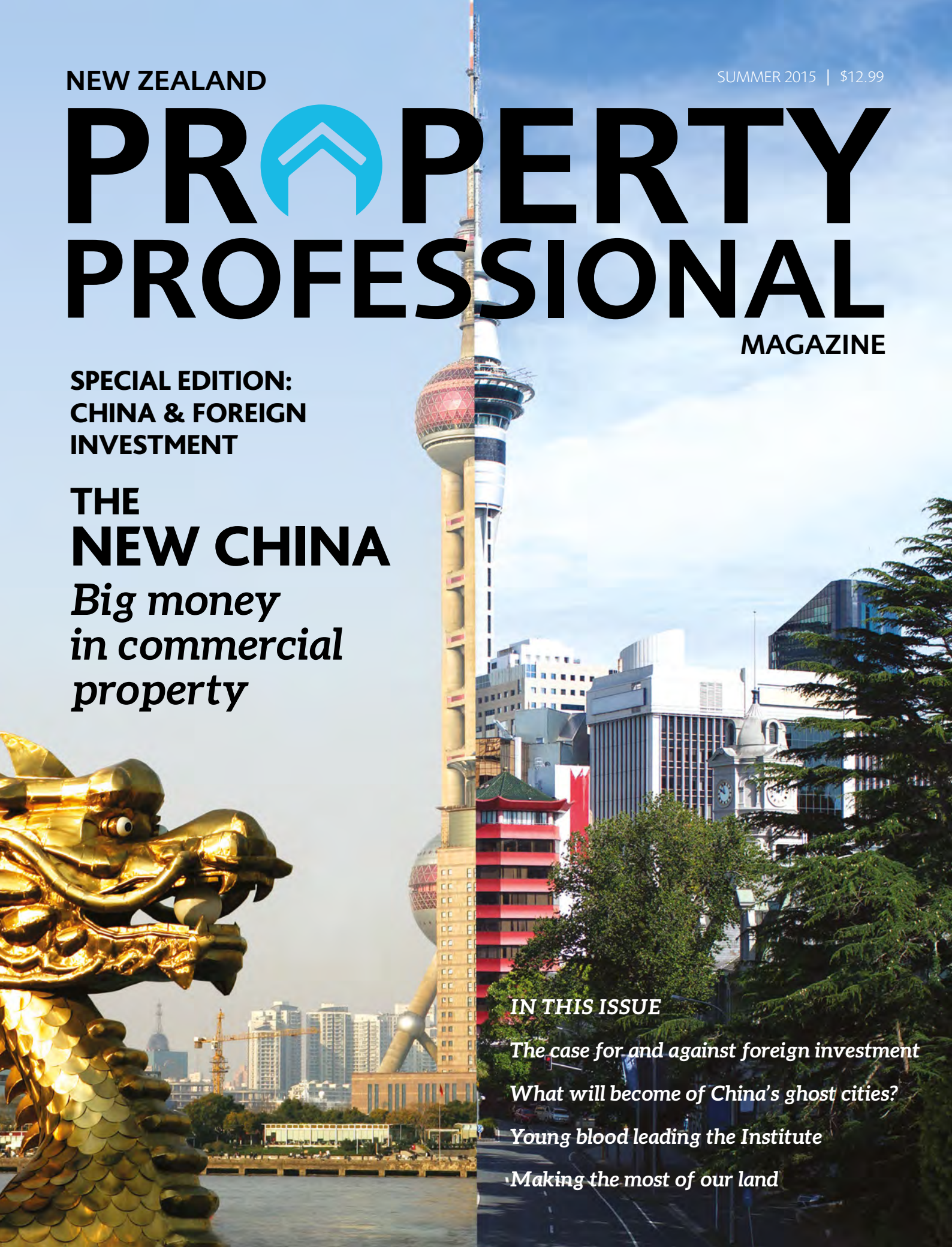
THE NEW CHINA

Big money in commercial property



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Young blood leading the Institute

Making the most of our land

Property is our Business

Simpson Grierson's national team of property specialists represent the interests of developers, vendors, purchasers, landlords, and tenants of all kinds of property.

We are unique – our property team focuses on property issues exclusively while other aspects of developments are tended to by our experts in construction, planning and financing.

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Simpson Grierson

THE GLOBALISATION OF PROPERTY

Ashley Church

You'd be hard pressed to find anything these days which hasn't changed as a result of globalisation. From the food we eat and the clothes we wear, through to the materials we build with – and our industry and professions are no exception. More and more, we're seeing property professionals employed by major international brands, working as part of a truly international team.

Regardless of who you work for – multinational, local or self-employed – it's only getting more vital for all property professionals to be aware of the international context in which we all work. Only recently, for example, we saw the Labour Party singling out Chinese investment as a driving factor in Auckland house pricing – an issue I was subsequently quite outspoken on, arguing that it's impossible to have a reasonable conversation on foreign investment if we single out one particular nationality rather than addressing all overseas investment equally.

Property features in international thinking at the highest level – you only need look at the Trans Pacific Partnership's inclusion of a clause specifically prohibiting the banning of foreign investment in housing to see how entrenched globalisation has become in the property world.

As the world changes, so too must the Institute. I'm committed to the idea that the Property Institute of New Zealand can't shut itself off from the world, and under my leadership we'll be concentrating on further strengthening of our international links. In the last few months alone, I've made a couple of visits to our colleagues at the Australian Property Institute (API), I've signed a memorandum of understanding with the Royal Institute of Chartered Surveyors (RICS) global CEO, Dr Sean Tompkins, and our former President Blue Hancock attended the World Association of Valuation Organisations (WAVO) annual congress.

All of these organisations, as well as a number of other partners like the International Valuation Standards Council (IVSC), represent opportunities for the Institute to cooperate with a like-minded body and in doing so better serve the needs of our (and their) members. By working together on education, events, policy and technology we are all collectively better placed to serve the interests of the professions we represent. I'd expect these relationships to deepen further over time, and I hope you'll see some concrete benefits coming from them reasonably soon.

As a side note – look out for the call for interest, in this edition of the magazine, for the 2016 overseas study tour. This is another great opportunity to learn from the property sector overseas and import that knowledge back to New Zealand, and we'd love to have you join us.

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THE NEW CHINA
BIG MONEY IN COMMERCIAL PROPERTY

Diana Clement

China once seemed a world or light years away. Today what's happening in commercial property in little known cities such as Wuhan, Ningbo or Bohai Bay can have a direct impact on the fortunes of New Zealand's economy and business.

Shanghai skyline *Photo: Jones Lang LaSalle*

Rapidly built cities

The scale of commercial property development in China is beyond imagination for many Kiwis. The great Yangtze and Pearl River deltas, for example, are forming vast networks of interconnected cities, notes Joe Zhou, Head of Research in China for Jones Lang LaSalle (JLL).

Shanghai, Zhou points out, is surrounded by more than 10 other cities with complementary economies that are forming an economic base many times the size of New Zealand. Billions of dollars is being poured into massive second and third tier cities many Kiwis also haven't heard of such as Tianjin, Dongguan, Chengdu and Hangzhou.

'What most Westerners fail to realise is how quickly China has built its cities,' says Simon Henry, co-founder of property listing website Juwai.com. 'Over the past 30 years, more than 500 million people have moved into its cities from farms. China now has 16 cities that are each larger than New Zealand's total population.' Its rapid urbanisation, and the growing sophistication of its economy, means a large and growing commercial property sector on a scale almost unheard of in any other country.

In Shanghai, for example, where Henry is based, new Grade A office buildings have come onto the market for the last 10 quarters in a row. There is now more than 5.5 million square metres of Grade A space just in Shanghai's CBD.

Can the growth continue?

The question on investors' minds is can the growth continue? There will, of course, be speed bumps. JLL is seeing a slowdown in second and third tier cities such as Wuhan and Ningbo, notes Zhou. One of the key factors in the slowdown is the 'rebalancing' from a manufacturing economy to a service economy and consumption, which is affecting different parts of the country at different rates.

Chinese commercial property is, of course, a huge and diverse market. What's happening in the mega cities of the big deltas is very different to a second or third tier inland city. What's more, there are different markets for logistics, retail, offices, hotels and other sectors.

Over the past 30 years, more than 500 million people have moved into its cities from farms. China now has 16 cities that are each larger than New Zealand's total population

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While China's growth has been stratospheric, the country is moving to a 'new normal' marked by lower, but more sustainable, economic growth.

JLL's *China60: From Fast Growth To Smart Growth* research suggests that supply is continuing unabated,' says Zhou, 'but in tier 2 and 3 cities an oversupply of office and retail is building up and could take two to five years to clear. The tier 1 cities such as Beijing and Shanghai, which are benefiting from the rebalancing of the economy, are not affected in the same way and those benefits will eventually filter to other parts of the country. While China's growth has been stratospheric, the country is moving to a 'new normal' marked by lower, but more sustainable, economic growth.

JLL tracks 60 top cities in China and says that despite the economic slowdown these lower tier cities are expected to contribute 15% of global growth over the next decade. Cities such as Xi'an, Guiyang and Kunming will benefit from a shift inland in the balance of economic activity.

Capital offshore to New Zealand

What is happening in the commercial property market in China isn't just academic for New Zealand, says Nick Tuffley, Chief Economist at the ASB. When slowdowns occur, as happened in 2015 thanks to the restructuring of the Chinese economy and falls in consumer demand, capital heads offshore and some of it finds its way to New Zealand.

That is a benefit for New Zealand which needs investment to cover its spending. 'We need capital from offshore to buy government bonds to fund our deficit, to fund a portion of the lending to (homeowners) and business, and to put that capital directly into businesses,' says Tuffley.

Mega experiments and trends

Growth in certain cities and hubs has been spectacular and the Chinese government is willing to take risks. It is unlikely Kiwis who don't do business with China will have heard of Qianhai. The free trade zone was announced in 2010 and the first projects built by 2014 with the aim of promoting strategically important service industries such as finance, logistics and IT and to open up Shenzhen to Hong Kong and abroad.

It is a test bed for the Chinese government to liberalise its currency and carry out financial reforms. Qianhai has proved so popular that rents in neighbouring Shenzhen have risen, according to the *South China Morning Post*, because thousands of companies that failed to find office accommodation in Qianhai have moved elsewhere in Shenzhen.

One of the early projects in Qianhai was the Enterprise Dream Park, which is modelled on Silicon Valley. The service industry cooperation zone, which is now four years into development, has proven successful according to research by Colliers International.

Risks

'Despite the maturing market there are still investment risks,' says Zhou. 'One is low transparency compared to overseas markets such as Australia, New Zealand and Europe.' There are also PR risks as the Tianjin Binhai New Area explosion showed a few months back. This huge explosion that killed 160 people and affected a wide area is expected to have longer-term economic impacts related to damage to Tianjin's image and reputation.'

There are also currency risks. Up until recently China's one-way path to appreciation was, for almost a decade, the icing on the cake for foreign inbound investors buying commercial property in China, notes Zhou. 'Currency appreciation by itself was insufficient to build an investment case, but was a welcome bonus – a boost to home currency returns. Although in most cases, the liquidity premium (the cost of exiting from the market) would erode most currency gains at the time of exit of the investment for foreign institutions.' China's devaluation in August had some consequences for investors and may have spooked some.

What's more, not all that China touches turns to gold, as many outside observers must believe. Ghost cities have emerged and showcase building has sometimes failed to combine function with place-building. The Zhengdong New Area and Chenggong District in China are examples of the kind of ghost cities that occur when this value is lacking.

There are also clouds on the horizon, thanks to consumers keeping their hands in their pockets and avoiding the malls. Westpac's

The Wanda Plaza Kunming Mall in China designed by Woods Bagot is one of 99 malls built by China's largest private developer *Photo: Woods Bagot*

MNI China Consumer Sentiment Indicator plunged by 7.2% to 109.7 in October 2015. That was the lowest value since the survey began in 2007. Even worse was the Business Conditions in One Year sentiment indicator, which fell 190.3% in the latest Westpac MNI survey.

This, combined with stock market volatility, led to a slower pace of corporate expansion in the third quarter of 2015, according to Knight Frank, commercial property agents in New Zealand, affecting Grade A office rents in particular. Knight Frank note that The People's Bank of China cutting interest rates and altering reserve requirement ratios to boost the economy had a direct impact on demand for Grade A offices in Beijing, Shanghai and Guangzhou, with Hong Kong not far behind.

As is the case almost everywhere in the world, the growing popularity of online shopping is affecting retail. According to Knight Frank, prime retail rents in Beijing and Shanghai in particular have been declining, although are stable in some cities such as Guangzhou.

In Beijing, prime office space is selling for USD$8,285 per square metre, with a vacancy rate of 5.8% and a yield of 6.4%, compared to USD$25,835 in Hong Kong, with a 1.7% vacancy rate but a 2.8% yield. ***(Table 1; p8)***

Likewise in the retail space, the price per square metre was USD$11,246 for Beijing, with a yield of 5.7%. ***(Table 2; p8)***

Not all that China touches turns to gold, as many outside observers must believe. Ghost cities have emerged and showcase building has sometimes failed to combine function with place-building.

Domestic and foreign investors

Chinese investors who got in early have made mega millions in the race to build the commercial centres of China. The name Dalian Wanda Commercial Properties comes up again and again. The company, which has built 99 Wanda Plaza shopping malls, grew from a small residential real estate firm in the 1980s to become the leader in Chinese commercial real estate. According to Forbes, its portfolio includes luxury hotels, theme parks and cinemas, and it holds assets in excess of $100 billion.

Foreign investors can and do operate in China, despite some constraints such as not being able to build golf courses. When China first opened up to foreign investment in the 1990s, Hong Kong investors led the way followed by other countries with large ethnic Chinese populations such as Singapore, says Zhou. Bit by bit capital began to flow in from other parts of the world.

Foreign mega investors do operate in China, including investment funds such as the Blackstone's Asia property fund and Macquarie funds such as the Macquarie Greater China Infrastructure Fund. 'Even so some foreign companies struggle even now to cope with the idiosyncrasies of dealing with Chinese bureaucracy and laws,' says Zhou. Where domestic investors understand

TABLE 1

Average prices, rents, vacancy rates and yields [1][2]

City	Price (US$ psm)	Rental (US$ psm per month)	Vacancy rate	Yield
Beijing	$8,283	$58.2	5.8%	6.4%
Shanghai	$8,885	$45.0	5.2%	6.1%
Guangzhou	$5,773	$28.3	15.0%	5.9%
Hong Kong	$25,835	$73.8	1.7%	2.8%
Taipei	$12,789	$24.5	10.2%	2.3%

[1] Average prices and rents are derived from different baskets of buildings, hence the two should not be used to estimate average yields. They are also not directly comparable among cities due to the different characteristics of each city.
[2] Prices and rents are calculated on gross floor areas.

Source: Knight Frank: *Greater China Property Market Report Q3 2015* (note this is for prime office space)

TABLE 2

Average prices, rents, vacancy rates and yields [1]

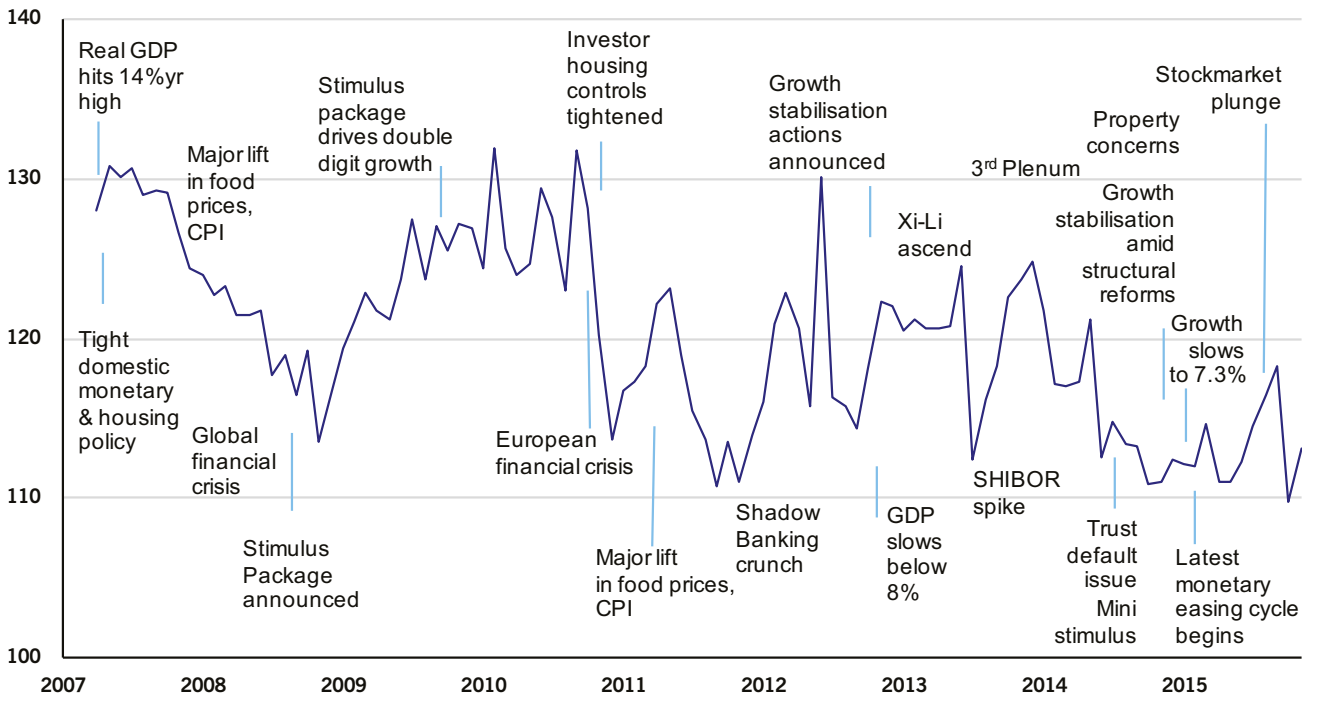
City	Price (US$ psm)	Rental (US$ psm per month)	Vacancy rate	Yield
Beijing	$11,246	$199.9	2.7%	5.7%
Shanghai	$35,378	$266.7	7.6%	6.4%
Guangzhou	$42,932	$271.0	4.2%	5.3%
Hong Kong	$281,748	$705.3	7.3%[2]	2.4%[3]
Taipei	$104,085	$188.0	n/a	2.1%

[1] Average prices and rents are derived from different baskets of buildings, hence the two should not be used to estimate average yields. They are also not directly comparable among cities due to the different characteristics of each city.
[2] End-2014 overall vacancy rate supplied by Rating and Valutation Department, HKSAR.
[3] Overall yield supplied by Rating and Valutation Department, HKSAR.

Source: Knight Frank (note this is for prime retail space)

GRAPH 1

Westpac MNI China Consumer Sentiment Indicator – Event Map



The currency devaluation, high prices and a weakening growth outlook have dampened interest from abroad recently.

how to push the 'leeway', foreigners often don't.

The currency devaluation, high prices and a weakening growth outlook have dampened interest from abroad recently. The devaluation made investors question future assumptions about cash flows on their China investments when converted into home currency.

This makes inbound investment into China worthy of a careful pause, notes Zhou. 'In limited cases new market entrants or capital raising mandates for China-focused funds may be delayed until a certainty can be achieved for managing returns and setting up partial hedging agreements. However, investors with China-focused mandates will continue to look at China. Foreign investors will likely wait and see, causing a temporary stall in decision making.'

FOREIGN MONEY IN PROPERTY: THE CASE AGAINST

James Shaw

The world is awash with cheap money and the New Zealand housing market is an attractive, safe place for cautious investors from overseas. Unfortunately, this is shutting Kiwi families out of the housing market and contributing to a serious financial stability risk in this country.

Auckland housing crisis

New Zealand has a housing problem or, to be more accurate, Auckland has a housing crisis. It is now one of the 10 most expensive cities to buy a house in, relative to income, in the world. Auckland house prices rise over 20% every year. The average price is steadily approaching one million dollars. I'm sure everyone reading this magazine is familiar with the figures.

I don't think there's a silver bullet to fix this. What's needed is a collection of tools to address the range of issues causing the problem, and someone in charge who isn't afraid to use them all. Building more affordable homes is a no-brainer; it simply must happen. Taxing capital gains in the same way all other income is taxed is also an important tool to target speculators and at the same time encourage local and international investors to invest in productive businesses. And so is limiting overseas investment in the property market.

Supply and demand

Of course, the root cause of the housing crisis is simple supply and demand. There just aren't enough houses in Auckland to keep up with the rapidly growing population or the hunger for investment properties. The government says Auckland needs at least 13,000 new homes every year, but only 8,700 were actually built in the year to September 2015. We're now into year three of the Auckland Housing Accord, for which the target is 17,000 new consents. We need more homes, fast, and the most efficient way to do this is through high-quality medium-density housing development along key transport corridors.

But while supply in Auckland is clearly a problem, the city's house price bubble isn't just a supply-side problem. The affordability problem isn't driven by owner-occupiers, it's driven by short-term speculators and longer-term investors. Theirs is the marginal dollar that would go somewhere else if not into housing.

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The most salient reason New Zealand should have a capital gains tax is that, without one, we've become a beacon for overseas investment in the property market.

Post-global financial crisis quantitative easing, historically low interest rates, and the entry of Russia and China into the global economy have created a vast sea of cheap globalised capital seeking safe harbours. According to the UK's Conservative Party think tank, the Bow Group, the global financial elite now numbers at least 15 million people, meaning that 'increasing housing supply can never bring down prices, no matter how much public land and green belt is turned into flats, because the demand for investment returns is almost infinite.'

Reliable data on the extent of overseas investment in Auckland is notoriously hard to find, but we do know that, domestically, over 40% of residential mortgage lending is for investment properties, according to the Reserve Bank. That doesn't give any reliable indication of the scale of overseas investment, but it does show that investors and speculators are a key contributor to the runaway Auckland housing market.

Capital gains tax

The Green Party is now the only remaining voice in Parliament calling for a capital gains tax, excluding the family home, as a tool to address this. Outside the Beehive's walls, of course, we're joined by the International Monetary Fund (IMF), the Organisation for Economic Cooperation and Development (OECD) and many of our own country's leading economists.

The capital gains tax debate was laid out in a previous issue of this magazine so I won't go into it in detail here, except to say that I think it's an important tool that any responsible government would use. Not just to cool demand from speculators, but also because it broadens the tax base and levels the playing field between people who work for wages and those who invest in property for income.

The most salient reason New Zealand should have a capital gains tax is that, without

one, we've become a beacon for overseas investment in the property market. Overseas investment isn't inherently bad, but it would be better to encourage investment into the productive sectors of our economy that create jobs and grow exports.

New Zealand an attractive option

Internationally, credit has never been this cheap. Many of the world's largest economies have in recent years undertaken quantitative easing – sometimes this gets referred to as printing money. There is a whole lot of cash flowing around the globe. If New Zealand wants to try to take little sips from this torrent, we're going to end up soaked.

Picture yourself as a would-be investor, maybe from a fast-growing economy. You've come into some money and you're looking for investment opportunities overseas. You don't like what you see in the commodities markets, because frankly, who would right now? They're just too volatile. Bonds are safe, but they're boring and they don't grow very fast. And then someone tells you about New Zealand.

New Zealand, they say, has one of the most stable economies in the world, built on producing high-quality food and exporting it to ever-growing markets. Its major banks all weathered the global financial crisis. It scores very highly on anti-corruption indexes and its governments change peacefully through open elections. You take a closer look and find that its companies are generally stable, but often they don't grow much and don't seem to attract much investment, which you take as a warning sign not to invest in them.

But Auckland's residential property market catches your eye. Twenty percent annual growth in asset values and no capital gains tax! Better still, record immigration seems to promise high housing demand for the foreseeable future.

A world-class education system is the decider – when your young kids are university age, maybe you'll send them to Auckland to study and they can live in the house, or one of the houses, that you're about to buy there. Sounds appealing, doesn't it? It doesn't take long for you, the hypothetical investor, to be browsing Auckland properties online and getting in touch with real estate agents.

Currently, the market signals are aligned to channel foreign money into residential property in Auckland.

I do not blame these investors at all. They're simply responding to clear market signals as most people would. It is up to the government to ensure that the market signals are aligned with New Zealand's interests. The National Government has clearly failed to do this.

Currently, the market signals are aligned to channel foreign money into residential property in Auckland. It's a safe haven for investors in a turbulent world. The end result is that when an elderly couple sells their family home, it's increasingly unlikely that a young family will be able to afford to buy it to live in. I would much rather that overseas investors were seeking out opportunities to invest in Kiwi businesses, helping them grow jobs and export to new markets.

Response of other countries

The UK is grappling with similar issues in its housing market, and policy-makers there are looking to Europe for solutions. Denmark prohibits investors from outside the EU from buying residential property, unless they've lived in Denmark for five years. Finland even restricts non-Finnish EU citizens from buying second homes in Finland. Other countries, such as Singapore, completely prohibit residential property sales to non-residents.

Wider economic implications

The other side of the housing crisis is less about families and where they live, and more about the big picture effects of an over-inflated housing market on the economy in general. As has been pointed out in this magazine previously, the fact that rents aren't rising nearly as fast as house prices suggests that a bubble is forming. Bubbles must burst, and when they do, it hurts.

Reserve Bank Governor Graeme Wheeler has said that the Auckland housing market is a serious financial risk because 'a sharp downturn could challenge financial stability.' I don't see a sharp downturn in the immediate future, but then again, the almost inevitable thing about market crashes is that people don't see them coming.

Retaining ownership in New Zealand

Just for the record, I couldn't care less where the overseas money comes from. When it comes to ownership of the strategic assets that underpin our economy – and land is certainly one of them – I think it's important that New Zealanders remain the owners.

The same applies to farms. Farming is the foundation of New Zealand's economy. We know from KPMG that most overseas investment is in the agricultural, energy and real estate sectors. We also know that in the last five years alone, farmland equal to nine times the size of Lake Taupo has been sold to overseas investors.

If we don't retain ownership of the strategic building blocks of our economy, the profits of our hard work and natural resources will end up disappearing overseas. No-one is arguing that we should cut off all overseas investment, just that we should make the right choices about where this investment goes to make sure it's creating real benefits for New Zealand.

And no-one is arguing that we shouldn't be building more houses to help fix the Auckland housing crisis. But just like you need more than one tool to build a house, we should be using the best tools available to us to fix the housing crisis. And one of those tools is reducing the ability of overseas investors to outbid local first home-buyers.

FOREIGN MONEY IN PROPERTY: THE CASE IN FAVOUR

Daniel Miles

Since our financial and economic coming of age in the 1980s, New Zealand has been consistently open to foreign investment, more so than virtually any other nation in the world. This article looks at the positive impacts of this practice in this country.

As a country, we went from being largely protected and closed off from the world in the early 1980s, and from a heritage of racial discrimination (think poll taxes on the Chinese), to a nation raw and exposed to the whims of global finance.

It'd be a gross misrepresentation of history to argue that the Douglas reforms of the 1980s were without controversy at the time, but as time has passed, the language of free trade and modern economic orthodoxy has increasingly dominated our politics – until lately. Spurred by soaring house prices in the Auckland market, New Zealanders are coming to question the value of foreign investment in our country and the value it brings.

Background

First off – you're reading the *New Zealand Property Professional* magazine. As such, it won't come as a surprise that we're focusing on foreign investment in property, not general foreign investment. Besides, despite the souring mood towards foreign investment in property, few would argue that a multinational firm opening a factory in New Zealand and employing New Zealanders is something we need to worry too much about.

The fears in New Zealand tend to revolve around property and land, and it's common to read accusations against the government of selling the country off piecemeal – accusations which reached new heights with the recent Trans-Pacific Partnership (TPP) agreement and its prevention of an outright ban on foreign land purchases amongst TPP signatory states. Labour added fuel to this fire by more or less committing to ignoring that provision, and proceeding with a ban regardless.

To lock out foreign investment would be a mistake, and New Zealand has a lot to be thankful for when it comes to this investment which, far from discouraging, we should be welcoming with open arms.

Daniel Miles is Communications Manager for the Property Institute of New Zealand. He has a background working in Parliament for both the National and Labour parties, as well as holding qualifications in economics and political science.
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ANTIQUES

If we ban foreign investors from purchasing land and property in New Zealand, all we do is remove competition for locally-based investors

Underlying issues

James Shaw's article in this issue of the magazine, setting out the Green Party's case against foreign investment, refers a lot to the underlying issues in the property market which make residential property an overwhelmingly attractive investment in comparison to other things – mostly the tax incentives for capital gains.

He's quite right that these underlying structural issues in the economy need addressing if we're to deal with the spiralling cost of Auckland housing – but quite wrong that foreign investment plays into this.

Fix the problem, not what looks like the problem

New Zealand public policy has a troubling tendency to skirt around issues rather than approach them directly. We've discussed both the Auckland property market and capital gains taxation respectively in depth in the last two editions of this magazine. The evidence suggests that Auckland's price issues are somewhat to do with undersupply, and primarily to do with demand to invest in a capital gain generating asset.

Laid out like that, the answer seems simple – enable more housing to be built, while simultaneously making residential property a less attractive investment. Removing overseas investors from the equation at first glance feels like it should work, but it fundamentally doesn't address the actual problem.

New Zealanders aren't dumb. We recognise an opportunity when we see it, and if a combination of our property market and our tax system allows us to pull in unusually high returns while also minimising our tax burden – well, people are going to do it. Added competition from foreign investors may have a marginal impact on pricing – a fact acknowledged at the Institute's recent keynote address by Ron Hoy Fong in Auckland – but there's more than enough money and appetite for investment in New Zealand already to escalate pricing to unsustainable levels solely due to the underlying issues.

If we ban foreign investors from purchasing land and property in New Zealand, all we do is remove competition for locally-based investors. The same problem as before continues unabated, but local investors are freed from overseas competition. There's simply no evidence to suggest that eliminating overseas investors will have any impact on pricing whatsoever.

Labour's Te Atatu MP Phil Twyford tried to make the argument that offshore Chinese investors made up a major part of Auckland's house purchases on the basis that 39.5% of sales transacted in data leaked from Barfoot & Thompson went to buyers with Asian sounding surnames (which would, obviously, also include the aforementioned third generation Kiwi investor Ron Hoy Fong). In response, Peter Thompson of Barfoots estimated that around 5-8% of sales went to non-resident Asian buyers. The fact is that we simply don't know what the numbers are in reality – but does it really matter? Is it really plausible to suggest that local investors are being outbid by hundreds of thousands at each auction? It seems much more likely that at best, a foreign investor winning at auction is only just edging out a locally-based investor, and thus having only a marginal impact on the price.

So we need to look at what our goal is. If we don't mind unsustainable pricing in the Auckland market, and only care about keeping those profits within New Zealand, then barring foreign investment will achieve that. If we want to solve the actual problem though, we need to approach it directly rather than taking short-term measures based on knee-jerk reactions.

Investors are vital

Let's not forget that property investors fulfil an absolutely vital role in the economy, and there's absolutely nothing wrong with property as an investment. Not everyone can afford to buy a house, not everyone wants to buy a house, and some people commute between cities and need more than one house. It's not realistic or desirable to eliminate renting, and we should welcome investors willing to provide that service to New Zealanders – regardless of where they live.

At the same time that eliminating foreign investors would help out local investors by lowering competition for properties, it'll also reduce the number of players in the rental market. So the same logic which says we might make properties cheaper for New Zealanders to buy, says all we might really achieve is making properties more expensive for New Zealanders to rent.

Value transfers, not vanishes

Another argument often made against offshore investment is that we're slowly but surely selling off our country. It's beguiling, but simply not meaningful. The implication is that we're handing away land and getting nothing in return – but nothing could be further from the truth.

In reality, capital is capital, and it gets invested or spent. Sometimes it's held in housing, where it provides a place to live for New Zealanders. Sometimes it's held in banks, where it fuels investment throughout the economy. Sometimes it's spent on consumer goods, and circulated through the economy. Property being sold offshore is simply converting one of these uses to another – instead of owning a house, that money might be invested in a business providing jobs, or in your child's education, or simply in a new TV

and boat – all manner of things which make New Zealanders better off.

We should feel the exact same way about foreign investment providing us with cash in exchange for property as we should about foreign investment providing us with jobs in exchange for labour, or goods in exchange for cash – it's all on the same spectrum.

The ethics of discrimination

Finally, there's the difficult question of ethics. Is it right to bar someone from buying land in New Zealand because they aren't a citizen? Unlike the rest of this article, which relies on facts and economic theory, this question is more vexed.

Okay, cards on the table here – while much of what I write for this magazine comes from my training and experience in economics, I'm from a politics background as well, and with that comes a whole lot of other personal views that I try to keep out of the magazine. But to avoid any allegations of bias, I'll declare that I've got a strong personal view that you shouldn't discriminate against anyone on the basis of something they can't control – ethnicity, gender, sexuality and, just as importantly, where they were born.

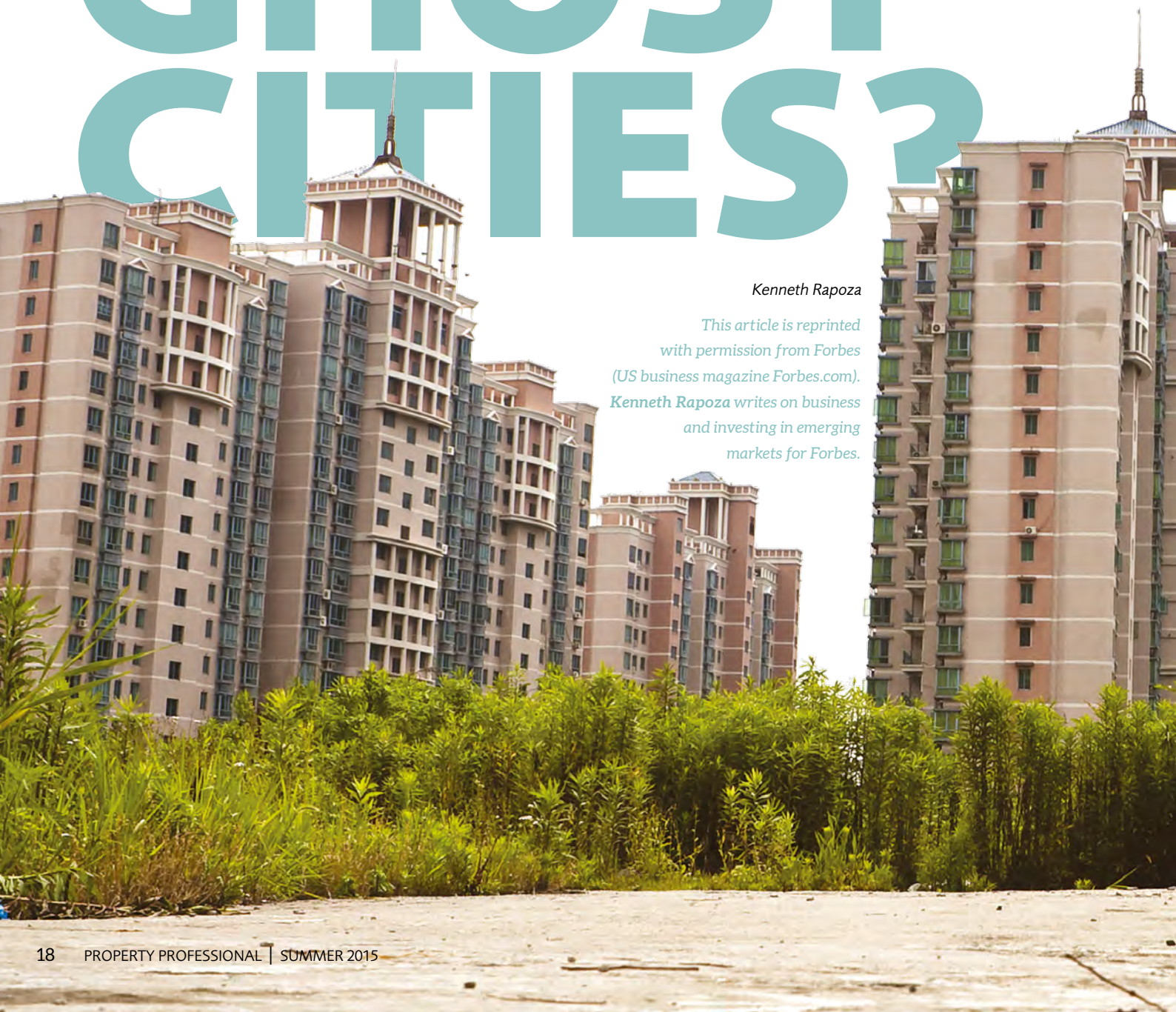
It's definitely possible to make a coherent argument that we should be keeping as much of New Zealand's economic sovereignty in our own hands. However – and I stress, this is very much a personal opinion – it just doesn't sit right to discriminate. To say that a foreigner can buy a shop which provides my job, but not a house which provides my housing – at the end of the day, what's the difference?

Solving the problem

At the risk of repeating, if we're ever to address the problem of runaway Auckland house prices, we need to target the tax incentives for investment. Targeting foreigners is at best missing the point, and at worst an exercise in racism which allows people to let out their inner dislike of the Chinese, or Indians, or another race altogether. Instead, we should place everyone on a level playing field regardless of race or nationality, and instead welcome anyone who wants to invest in providing for New Zealanders – be it jobs, products, or even housing.

To say that a foreigner can buy a shop which provides my job, but not a house which provides my housing – at the end of the day, what's the difference?

WHAT WILL BECOME OF CHINA'S GHOST CITIES?



Kenneth Rapoza

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Little did we know that most of that iron ore being shipped to Guangzhou from Rio de Janeiro and Port Hedland, Australia was going to build Chinese cities; cities that would remain vacant for years.

China single-handedly topped the phrase 'bridge to nowhere' and made ghost cities a euphemism for lousy development planning in the world's No. 2 economy. Anyone can build a useless overpass, but it takes China to build a city for a million people with no buyers in sight.

The naysayers loved the Western media's discovery of China's ghost cities. It was evidence that China's growth of the last 20 years was based on building things nobody needed or wanted. This was planned obsolescence on a grand scale. And now that the economy is slowing, what will become of those cities? Many of them are debt burdens carried by the developers who haven't sold a single unit.

From shopping malls to soccer stadiums, hundreds of new cities in China are largely empty. And yet more cities are still being built deep in the heart of the country. All in hopes that its rural population will one day move to a flat in a city without a mayor. It's plausible, of course. That's because over the next 15 years, the country's urban population will be one billion; three times that of the US.

What will become of these cities going forward? Here's a quick answer: a handful might be shuttered. Most will be filled. New ones will undoubtedly be built.

China's developing its urban architecture three ways: new cities (xinshi), new districts (xinqu), and the so-called townification (chengzhenhua). Townification is quite a departure from the way Chinese cities have developed to date. This is the transformation of small rural centers and even tribal villages and building a small urban center around them. The Communist Party planners in Beijing want to urbanize over 100 million rural Chinese over the next five years alone. That would require the construction of 50 Bostons, or six Shanghais, by 2020.

> *From shopping malls to soccer stadiums, hundreds of new cities in China are largely empty.*

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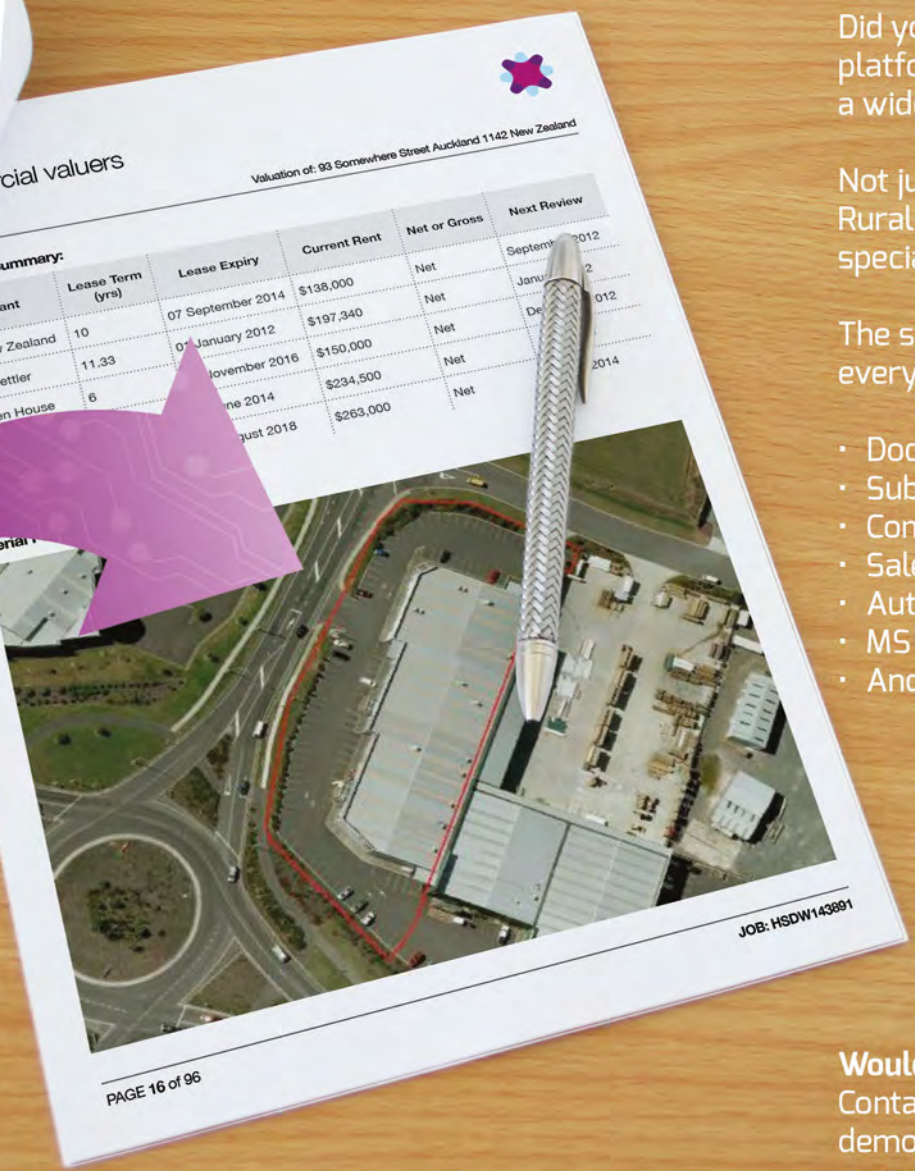

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China's ghost cities are, and were, a harbinger of the country's real estate bubble.

Townification is lower intensity than that. These are small cities rather than skyscraper zones designed to house suits and high heels. It's more widespread than traditional urbanization, and will define the way China develops socio-economically over the coming years.

Roughly 40% of the 300 million Chinese expected to move into a city by 2030 will mostly be moving to smaller cities in the 'chengzhenhua' system. Rather than migrating to cities, the cities will be built around them instead.

Tattoed hipster and Silk Road traveling journalist Wade Shepard calls this the largest social experiment that has played out in human history. Shepard is the author of *Ghost Cities of China*, a readable explanation of what's going down in China's new downtowns.

Creative destruction then and now

In 2010, the governments of Shanghai and Beijing invested nearly $60 billion to bring the World Expo to Shanghai. They kicked people off their land. All told, 18,452 households got eviction notices. Some 270 factories had to move. China's 'stroke-of-a-pen' economy can change fortunes just like that. Those who complained about the relocation program were arrested in typical Chinese fashion. The focus of the Expo was 'Better City, Better Life', but ironically, what it left behind was a ghost town. When it was over, Shanghai was left with a swathe of land the size of Monaco with absolutely nothing going on. Many of the buildings were demolished. In the words of Dutch architect Harry de Hartog, 'It is still a big empty wound in the city of Shanghai.'

There is a blip of activity there, near the Expo museum. Getting to it requires walking for 20 minutes through a desolate, post-urban landscape. It's taken five years before change has come to town. The area is now one of four key development zones in the city's current five year plan, and a $483 million project is in the works to turn it into a mixed-use district, with shopping, restaurants, entertainment, and Shanghai's third business center. Office towers and apartment buildings are already under construction.

'It's going to become a high-end destination,' says Pierluca Maffey, a project manager for US based John Portman & Associates, one of the firms of architects working on the site. China's ghost cities are, and were, a harbinger of the country's real estate bubble. It's also part of the narrative that says Chinese municipalities are spending money on projects with no possible return on investment. But seeing how many of these loans are from the state, and the state is mainly concerned about job creation, building for the sake of the future and for present jobs actually worked. For a while. It might not work going forward and so there will be less creative destruction, and more creation.

When Shepard set out to investigate China's ghost towns he was a student at Zhejiang University. When he brought the issue up with his professors, they told him 'those places are everywhere.'

'There was something about that phrase – those places are everywhere – that kept me locked on the topic,' he says. 'Later that year I drove off a highway into a deserted portion of Erenhot on the Mongolian border, a place that would later become infamous as the ghost city reports in the Western media. I walked through sand strewn empty streets out in the Gobi desert. It became clear to me that something big was happening here.'

Happening is the operative word. Because it is still happening.

The phantoms of China

There are megacities inside of megacities with sprawling poverty in between. The government wants to do away with this. Instead, if one can envision a megacity with tentacles reaching out and ending in circles of much smaller cities, then this is the future of China. This is what the late 21st century will look like. China is building for this. Meanwhile, what's already been built remains vacant, or under-populated. Some people don't mind.

Along the outskirts of Shanghai there is a town built near a Volkswagen plant. It had everything: housing, parks, canal-side

Empty square and skyscrapers of Shenzheng in China

promenades, benches, shops, roads, statues and office buildings. The only thing it lacked was a population. Shepard recalls visiting Anting German Town, a Bauhaus-style town that looks like it belongs in Hamburg. There was a bartender there. And his wife. And the VW factory workers that came to his bar after work to drink.

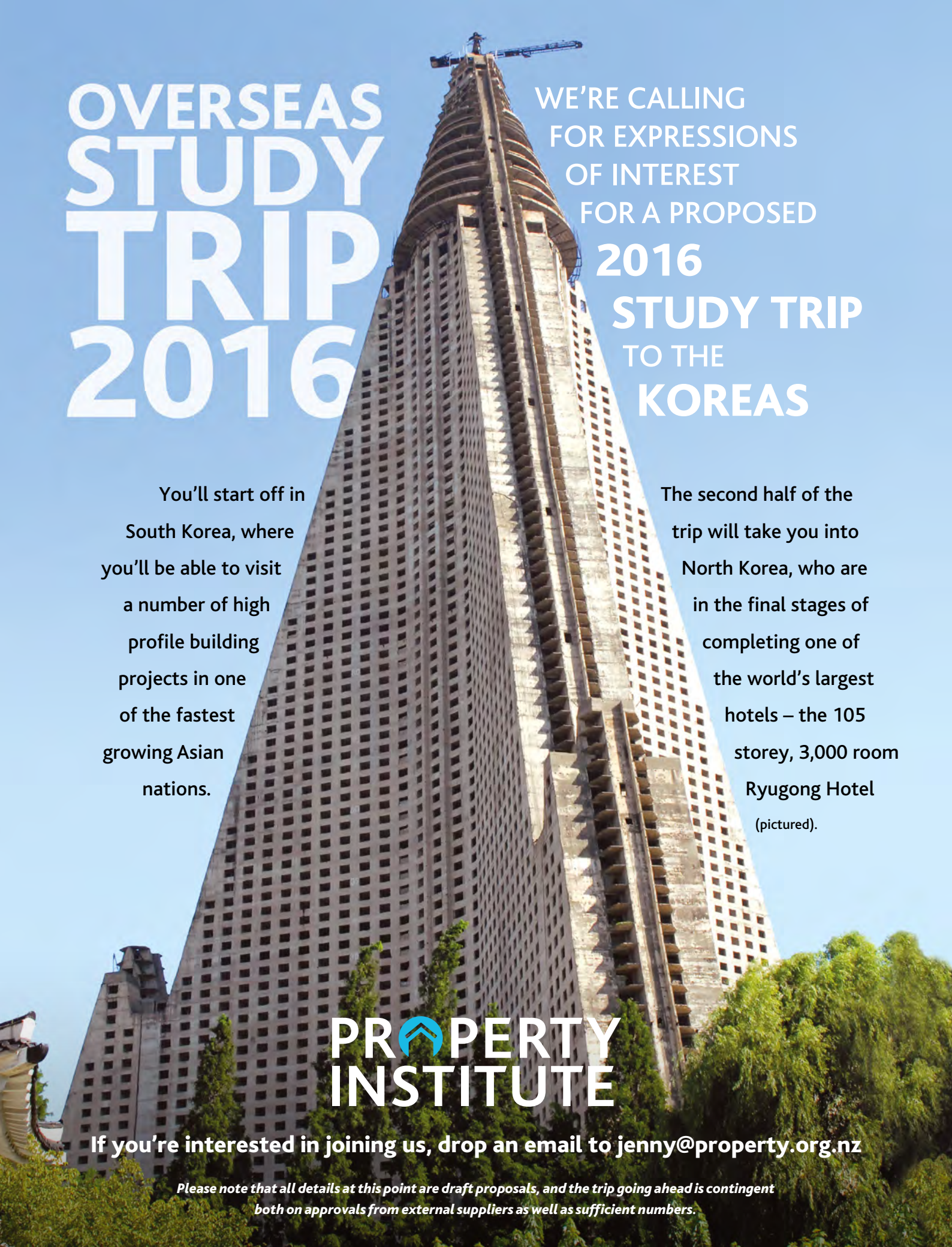
'When I asked the bartender's wife (left unnamed in the book, so we can trust his account or not) if she thought more people would come to Anting, she replied with certainty that they would.' Others interviewed in the book didn't seem too worried about the lack of population. They seemed to revel in it. Clean, orderly, no shanty towns towering over you. Not as expensive as Shanghai. What's not to love?

China's continued urbanization push can be viewed as a full-on effort to develop an insulated economy that's based on domestic production delivering goods and services to domestic consumers. Past crises in Europe and the US have taken their toll on the Chinese economy. During the US Great Recession, China had to bail out the economy to the tune of nearly a trillion dollars. Its GDP fell below 7%. It was, alas, the hard landing the popular pundits had been waiting for. To curb the impact that foreign financial meltdowns can have, China has performed a U-turn and is now looking inward. In 2013, the service economy topped manufacturing for the first time. City building goes along with this.

Not every new city or urban expansion project will succeed. Some will fail and become true ghost towns, the kind that remind us Westerners of cowboy lore, complete with Gobi desert tumbleweeds. But to measure the vitality of this ambitious project, one needs to counter-balance failures with successes, Shepard reminds us. By focusing on the extreme and often confusing aspects of China's urbanization movement, the real China story gets lost in the noise. Although the past is not indicative of the future, let us not forget that this country pulled more people out of dollar-a-day poverty than any other country. Many of those riches came from building new cities. In the last two decades, China has built an entirely new country, one that matters to Apple as much as the US; a country whose businesses own American brands like AMC Theaters, and are building high rises in Los Angeles.

China's continued urbanization push can be viewed as a full-on effort to develop an insulated economy that's based on domestic production delivering goods and services to domestic consumers.

Shepard's work here is ultimately a solid journalist's diary, complete with reference index and source interviews. His work is based on years spent wandering the city streets of China with the locals, not a foreign camera crew of first-timers. If you want opinion from pundits, or first-take thoughts from a reporter parachuting in for a stint in Kangbashi, the Mongolian border town that became the poster child of China's jacked-up bridges-to-nowhere, then *Ghost Cities* is not your thing. But for readers looking for a more reasonable, honest broker on the topic, then Shepard is your guy.



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PROPERTY INSTITUTE

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Please note that all details at this point are draft proposals, and the trip going ahead is contingent both on approvals from external suppliers as well as sufficient numbers.

YOUNG BLOOD
LEADING THE INSTITUTE

Kelly Beckett

History

The Property Institute Young Leaders Group was formed in April 2013 to provide a succession plan for the Institute and to invest in its future leaders, as well as recognising that it needs to support the needs of its diverse members and operate in this global and challenging environment. The programme gives up and coming members of the Institute first-hand exposure to the governance of their professions and the inner workings of a professional organisation. We aim to be involved in strategic and operational projects at a governance level and try to add a younger perspective and develop the way the Institute looks at these problems. We are a self-managed group and report back to our respective committees.

The Young Leaders Group for 2013-2015 consisted of seven members from throughout the country. Katie Grindley was our representative on the PINZ Board and I was the representative on the NZIV Council. The remaining members held positions on the key national committees. Jay Sorensen is a member of the Standards Board, Jeremy Ball is on the Property Advisory Council, Nicole Owen is on the Property Management Council, Craig Russell is now the chair of the Finance and Risk Committee and Aimee Martin is on the Education Committee.

Our projects

As the former chair of the 2013-2015 group, I'd like to take this opportunity to outline the projects we've been working on for the last two years. Arguably our most valuable project was when we ran a focus group discussing the proposed changes to the Valuers Act 1948 to gauge the younger members' perspective. We ran roadshow meetings on the Valuers Act Review on 15 July 2014 in Auckland and on 16 July 2014 in Wellington and Christchurch, respectively. Our intention was to generate discussion and obtain perspectives from young valuers working throughout the country.

We targeted and invited specific people to attend. Over 20 people attended the Auckland and Wellington roadshows, respectively, with a further eight attending in Christchurch. All meetings including a range of both registered and unregistered valuers. We ran a discussion-style session which relied heavily on those in attendance participating. Surprisingly, the feeling was largely unanimous at these workshops. We then took the findings back to the Valuers Council and had heavy input into the NZIV submission in addition to writing our own.

Our initial focus was on the promotion of PINZ within the community and, in particular, to schools and universities to promote 'property

The programme gives up and coming members of the Institute first-hand exposure to the governance of their professions and the inner workings of a professional organisation.

Kelly Beckett is a Senior Valuer with CBRE based in Auckland and was the Valuers Council Representative on the Young Leadership Group.
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as a career'. We contacted over 30 schools throughout the North Island and have been providing resources to them, and have also presented to a number of these either at their career expo events or to assemblies or various classrooms. We have set up a database of who we contacted and what their respective responses were, if we received one. This has been particularly well received in the provinces with Jay, Jeremy and Craig all presenting regularly to local schools. Uptake in Auckland was very poor, and frankly disappointing, but I suspect that is partially the result of having better access to resources and information in the form of careers advisors, career expos etc.

We have designed and printed a brochure outlining options available held under the PINZ banner and prepared a 30 minute power point presentation on what a career in property entails.

Nicole also attended a careers event at Victoria University in 2014. We have also established relationships with Massey University and Auckland University.

Our projects have also included improvements being made to the website, including more information on advancement through the different levels of membership of PINZ, and we have developed a careers page for schools. As you'll be aware, the website is now being fully redesigned and our content will form a key part of that.

We've also published numerous articles in the *Property Professional* magazine and contributed content for the online modules we have prepared to assist valuers working towards registration.

We are also actively involved at a local level to engage members and answer their concerns.

I would strongly encourage the new members to become part of your local branch committee.

A number of our current group members also serve on their local branches. I would strongly encourage the new members to become part of your local branch committee. Not only will it provide you with a good background into governance, but it also provides another platform on which to deliver your projects.

We will continue in a mentoring capacity for the new members. It is our intention that the new group will continue to build on the projects we have established as well as creating their own.

The outgoing Young Leadership Committee and the new incoming committee with Ashley Church (CEO of PINZ).

From left: Ashley Church, Luke van den Broek, Craig Russell (rear), Andrew Liew (front), Jay Sorensen, Katie Grindley (front), Susie Penrose (rear), Helen Brumby (rear), Kelly Beckett (front), Nicole Owen, Jeremy Ball, Benjamin Gill.

THE NEW GROUP

The new group for 2015-2017 has been selected and they officially took over their roles at the PINZ AGM held in Christchurch on 3 June 2015. We received over 30 applications for this intake. Thank you to all those who took the time to apply. The calibre of applications received was very high. The new group consists of:

Luke van den Broek

PINZ BOARD REPRESENTATIVE

Luke is a Registered Valuer at Quotable Value. He attended Massey University where he completed a Bachelor of Business Studies majoring in Valuation and Property Management and Agribusiness. Since graduating in 2009 he has been employed at Quotable Value and was registered in 2012. Luke is now the Canterbury Rating Manager. In this role he leads a team of valuers to deliver fair and equitable rating valuations for nine territorial authorities across the Canterbury region. Luke has previous experience with the Property Institute as a past Waikato branch committee member and Chair, and is currently a member of the Canterbury/Westland branch committee.

Helen Brumby

PROPERTY AND FACILITIES MANAGEMENT

Helen is a Property Manager for APL Property Rotorua who specialise in commercial property management and consultancy within Rotorua and the surrounding regions. She obtained a Bachelor of Business majoring in Valuation and Property Management from Massey University in 2008. In addition to being a full member of PINZ, Helen is in her fifth year as the Chair of the Rotorua /Taupo branch. In her seven years with APL Property, she has undertaken a wide range of consultancy and management including portfolio oversight of Maori land, as well as project management of building upgrades and building condition assessment surveys for the Ministry of Education and other private clients. While focused predominantly on commercial property, Helen has a particular interest in sustainable buildings.

Andrew Liew

INFRASTRUCTURE, PLANT AND MACHINERY

Andrew is a Plant and Machinery Valuer for Beca Ltd. Andrew completed a Bachelor of Commerce majoring in Valuation and Property Management at Lincoln University. Since graduating in 2009 he has worked in property and facilities management for retail and industrial properties nationwide before becoming a valuer at Turners Auctions and Beca Ltd. Andrew has undertaken valuations ranging from industrial to infrastructure assets as well as condition assessment surveys for local authorities and companies throughout Australasia. He is an Affliate Member of PINZ and is currently working towards gaining his registration as a Plant and Machinery Valuer.

Susie Penrose

VALUERS COUNCIL REPRESENTATIVE

Susie is a Registered Valuer, working predominantly in the commercial/industrial sector, but carrying out a range of other work including valuations in the accommodation and aged care sectors, iwi treaty settlement claims and client advisory work in both the Hawkes Bay and the Gisborne area. Susie joined TelferYoung (Hawkes Bay) Limited in 2009 after completing a Bachelor of Business Studies (Valuation and Property Management) degree at Massey University in Palmerston North, and gained registration in 2014. She is currently on the Hawkes Bay Branch of PINZ and is the Chair of the TelferYoung Young Valuers Focus Group.

Benjamin Gill

PROPERTY ADVISORY

Ben is currently the Programme Manager for Housing & Accommodation Assistance at the New Zealand Defence Force and is based in Wellington. He works in an advisory capacity providing strategic direction for the Defence Force housing estate. Ben previously worked for the Education Infrastructure Service (Ministry of Education) in New Zealand. He graduated from the University of Birmingham with a BSc Economics (Hons) and completed a MSc Housing Development with the University of Glasgow. Ben is currently studying towards an MBA Construction & Real Estate (Accelerated Route) with the College of Estate Management, University of Reading and is an Affiliate Member of PINZ.

Congratulations to these new members on their appointments. We look forward to seeing what this group will achieve over the next two years. Finally I would like to thank the Property Institute for their support and for providing a platform for younger members to get involved at a strategic level.

MAKING THE MOST OF OUR LAND

A REVIEW OF THE PRODUCTIVITY COMMISSION'S REPORT

Allan Smee

This is a follow up to the first article in the September issue on the Productivity Commission Report on Use of Land for Housing, which was released on 21 October 2015.

Reaction to report

Although this report was widely anticipated, there has been little media attention on its release, which was overshadowed by the recent release of the Parliamentary Commissioner for the Environment State of the Environment Report. It is also interesting to note that later announcements of some key issues mentioned in the first article have failed to reference the report.

Auckland Housing Accord Monitoring Report

Since the report was released, there have been two major announcements from the government. The first of these was the Auckland Housing Accord monitoring report of 26 November 2015. The report, released jointly by the Hon Nick Smith and Mayor Len Brown, indicated that the Housing Accord was on track with '23,806 dwellings consented and new sections created, as compared to the target of 22,000.' The Mayor also indicated that the Accord has seen the establishment of 97 Special Housing Areas, with a further nine announced recently, and he says this has the potential to lead to the construction of over 48,000 homes.

Although the number of new dwelling consents and the potential of 48,000 houses from these Special Housing Areas is impressive, there needs be some caution. It important to note that only 15% have earthworks underway and only 22% of the proposed housing is under construction. The remainder are either in the design phase (20%), have resource consent applications underway (29%) or have resource consents lodged or approved (14%). It appears that both central government and Auckland City are possibly counting their chickens before they hatch, as not all consents end up with a completed dwelling, so these figures should not be taken at face value.

It should also be noted that the establishment of the legislation to develop Special Housing Areas is effectively a temporary measure until the Auckland City Unitary Plan is completed on schedule in October 2016. Dr Smith indicated that the government would need to continue to assist the Auckland City housing issue through the development of 'new housing on Crown-owned land in Auckland, supporting the council in the completion of the new Auckland Unitary Plan, consulting on a new Urban Development National Policy Statement, and reform of the Resource Management Act.'

Although the number of new dwelling consents and the potential of 48,000 houses from these Special Housing Areas is impressive, there needs be some caution.

To aid in this, the government passed legislation enabling additional commissioners and multiple hearings panels to help facilitate the panel reporting the plan back to the council on time. There was no mention of the Productivity Commission report, whose primary position was the establishment of Special Housing Authorities who would play an active role in housing development.

Resource Legislation Amendment Bill

A second major announcement was the Resource Legislation Amendment Bill, which has been introduced to parliament and passed it first reading. The 180-page Bill comprises 40 changes contained in 235 clauses and eight schedules. It makes changes to the Resource Management Act 1991 (RMA), the Reserves Act 1977, the Public Works Act 1981, the Conservation Act 1987, the Environmental Protection Authority Act 2011 and the Exclusive Economic Zone and Continental Shelf (Environmental Effects) Act 2012. The changes mainly focus on the RMA and the following four are the most significant:

- Requiring councils to follow national planning templates that will improve the consistency and reduce the complexity of plans. This will substantially reduce the volume of planning documents across the country because most provisions will be standardised.

Allan Smee is the Research and Information Manager for the Property Institute of New Zealand. He has a background in data analysis and academia.
***e**: allan@property.org.nz*

Another major change is a move to a faster and more flexible planning process consisting of four tracks.

- Faster and more flexible planning processes. The Bill provides three different tracks by which a council can produce a plan: the existing track that now has tighter timelines, a new collaborative track and a streamlined track.
- Reduced requirements for consents. The Bill eliminates the need for thousands of minor consents by giving councils discretion to not require them, by introducing a new 10-day fast-track for simple consents and by removing requirements for consents where they are already required under other Acts.
- Stronger national direction around requiring provision for growth like housing, and for national regulations to address issues like dairy stock in rivers and other regulations to limit the extent of RMA application.

National template timing

The introduction of national templates for resource management plans and policy statements will reduce confusion and make plans easier and cheaper to use and review. But the introduction of these templates will take time to implement as a number of council planning staff are currently undertaking plan reviews or have completed them already. For example, the Auckland City Unitary Plan is well underway and it would be difficult to adopt a new template three-quarters of the way through the process. Requiring councils to adopt these national templates would place additional strain on their planning departments, so it would be surprising to see this implemented within the next two to three years.

Fast-track planning process

Another major change is a move to a faster and more flexible planning process consisting of four tracks: the existing process with tighter timelines, a new collaborative track, a streamlined track, and a new 10-day fast-track for simple consents.

The new streamlined planning process will mean councils can formally ask the Minister for the Environment for a plan-making process that suits their local circumstances. In the past, the government has sometimes had to pass special legislation where the existing planning process would have been too slow, such as in Auckland and Christchurch. The new streamlined process will reduce the need for this kind of ad hoc law-making. There is little information on what could constitute the requirement for this planning process. The Christchurch earthquake and Auckland housing issues could be considered unusual events, so it will difficult at this stage to determine how this category would be applied.

The changes introduced in the Bill mean councils have to be more forward thinking, and proactively plan to have enough residential and business land for development.

Collaboration vital

The collaborative planning process encourages greater front-end public engagement. It will help people with different views to work together to resolve resource management issues, which will reduce litigation costs and lengthy delays. The collaborative planning process gives the local authority control over which project will be subject to this planning process, including the:

- Establishment of a collaborative group, appointments to be made, the group's terms of reference, and publicity requirements (new clauses 39 to 42)
- The reporting requirements for a collaborative group (new clauses 43 and 44)
- Obligations of the local authority responsible for establishing the collaborative group, including the preparation of a proposal (new clauses 45 to 50, 54, and 56)
- Obligations of the collaborative group in relation to the role of a review panel (new clause 52)
- The establishment and role of a review panel, and its functions and powers and procedural matters (new clauses 51, 53 and 63 to 73)
- Rights of appeal under the collaborative planning process (new clauses 58 to 61 and Schedule 2).

This effectively places the local authority in full control of the process, and it remains to be seen how this effectively removes barriers and speeds it up.

Iwi consultation

In addition, the local authorities are to increase consultation with iwi overall and to do this earlier in the plan-making process, including inviting iwi to form an Iwi Participation Arrangement. This arrangement will set out how a council will engage and consult with iwi when developing or changing plans, and will include provision for any existing engagement processes set out under specific Treaty settlement legislation.

Other changes in the Bill

The Bill also aims to make consent processes more simple and efficient by identifying the parties eligible to be notified of different types of applications. In particular, it refines the notification regime and introduces limits to the scope and content of submissions and subsequent appeals, which should speed up the existing process.

The Bill also introduces a 10-working-day time limit for determining simple applications (fast-track applications) and allowing councils to treat certain activities as permitted. This fast-track process is for minor activities, meaning a homeowner extending a deck only has to consult the affected neighbour. Councils will have discretion to not require resource consent for minor issues. Also, councils will be required to have fixed fees for standard consents so that homeowners have certainty over costs.

Constraint on land supply for housing

The only other major factor is a change to the constraint on land supply for housing, which was identified by the Productivity Commission who had found the planning system isn't responsive enough for a rapidly growing population or increased demand for housing. The changes introduced in the Bill mean councils have to be more forward thinking, and proactively plan to have enough residential and business land for development.

An example of this is the change to the presumption that land may not subdivided unless the subdivision is expressly allowed by a national environmental standard, district plan rule or resource consent. The new presumption will be that land subdivision will be allowed unless it is restricted.

Additional compensation

Another major change introduced is one to the Public Works Act, which sees an increase in the solatium compensation payment for disruption, interference and other inconveniences. The solatium has not been increased from $2,000 since it was introduced in 1975, and the reforms will increase the amount up to a maximum of $50,000 which will be determined by the Crown. In addition, there is a new compensation for landowners whose land (but not their home) is acquired – of up to $25,000. Both these amounts are in addition to the market value based compensation.

Timeframe slow

These changes could have major impacts on the development process and could solve a number of issues. The only problem will be the timeframe for their introduction and passing of the Bill into law, and I believe we are looking at least two to three years before any major benefit will be seen.

AUCKLAND WATERFRONT DEVELOPMENT AGENCY v MOBIL **LESSEE DECONTAMINATION OBLIGATIONS**

Nick Wilson

The Court of Appeal surprised some with its ruling earlier this year in Auckland Waterfront Development Agency v Mobil Oil New Zealand Limited [2015] NZCA 390, by overturning an earlier High Court decision and ordering Mobil (a vacating lessee) to pay $10 million towards the costs of sub-surface decontamination.

The judgment of the Court of Appeal, and the earlier High Court judgment, provide helpful guidance on how a court will intepret make good provisions under a lease. The judgments are a useful reminder of the importance of ensuring that the drafting of your leases is as clear and unambigous as possible. It is not always suitable to rely on the boilerplate provisions of a 'standard' lease. Analyses of the two judgments are summarised below.

Background

The case related to land at the Tank Farm on Auckland's waterfront, which had been used for oil storage by various oil companies since the 1920s. When Mobil vacated the land in 2011, it was found to be severely contaminated from years of oil spillage.

'Clean and tidy' provisions of lease

Both the judgment by the Court of Appeal and the earlier High Court ruling from 2014 centred on the interpretation of 'clean and tidy' provisions in 1985 leases. These provisions required Mobil to:

> ... at all times ... keep the said land ... in good order and clean and tidy and free from rubbish, weeds and growth ... and deliver up ... the said land and any improvements left thereon in such good and tenantable repair and condition and clean and tidy to the reasonable satisfaction of the Board.

The Auckland Waterfront Development Agency (AWDA), which, since termination of the lease had redeveloped the land for mixed residential, commercial and retail use, argued that the lease required Mobil to fully decontaminate, including removing historic contamination caused by earlier occupiers of the site and other neighbouring properties.

Mobil Oil New Zealand Limited (Mobil), on the other hand, argued that the make good obligations in the lease were never intended to require removal historic contamination and to place the surface condition or appearance of the land into a clean and tidy state.

2014 High Court ruling

Judge Katz in the High Court favoured Mobil's argument and found that the lease did not require the company to decontaminate. In interpreting the wording of the clause, she found that the natural and ordinary meaning of the clause (in isolation) was 'not apparent'. Judge Katz proceeded to consider a wide matrix of facts in interpreting the parties' intentions:

- The pre-contract negotiations and post-contract conduct of the parties, each of which are admissible to establish the party's knowledge of relevant circumstances and provide a setting in which they used the relevant words in the contract.
- Much of the contamination had already occurred at the time of Mobil's original lease (in the 1950s). The judge thought it would be unusual for a lessee to agree to be responsible for remedying damage caused by another.
- The earlier leases placed no obligation on the lessee to decontaminate. In order to change that policy, the judge felt there would need to be clear and unambiguous wording in the lease to record the change in position.
- The 1980 leases were short term. The judge felt that the shorter the term the less likely that an onerous and expensive repair obligation would have been intended.
- The common law doctrine of 'waste', which generally provides that a lessee cannot damage or alter the lessor's interest in the land, was considered. In this case an action

When Mobil vacated the land in 2011, it was found to be severely contaminated from years of oil spillage.

for waste was time barred and so the only avenue open to AWDA to recover costs for decontaminating was to sue Mobil under contract, i.e. under the terms of the lease. The judge found that even were a claim under the doctrine of waste available, that Mobil would have a defence against any such claim of 'reasonable use' because the use of the land for *oil storage* was permitted under the lease.

- AWDA noted the obligation to 'keep' the land clean and tidy, and argued this inferred an obligation to make sure that the land is clean and tidy on commencement and if necessary to make it so. The judge considered this would have been a significant undertaking for a lessee to immediately decontaminate at commencement and that it would have been unusual for the lessee to agree to such an obligation.
- Mobil and other Exxon Mobil entities had occupied the sites since the 1920s to 1930s. AWDA claimed it was not unreasonable to have intended that Mobil would restore it to its former condition, but the Court distinguished the current lessee from those earlier lessee entities.
- The UK case law (the *Anstruther* authorities) was analysed. This line of authority provides that a lessee's standard of make good will apply to the standard of the premises as at the commencement of the lease. It was found that heavy industrial use was the anticipated use of the land at the time of the commencement of the 1985 leases, and if there was a make good obligation under the lease, it would only be to this lesser industrial level standard and not the full decontamination that AWDA was arguing for.

2015 – Court of Appeal reverses finding

The Court of Appeal has now overturned Judge Katz's decision and instead found that Mobil is liable for fully decontaminating. The key points in which the Court of Appeal differed in its interpretation of the 'clean and tidy' clauses follow.

The Court disregarded the fact that there were different entities that occupied the site prior to 1952, noting that the original leases (from 1925 and 1927) were assigned to different entities which ultimately became part of Mobil NZ. In the Court's view, Mobil had inherited these earlier occupants' liability under the previous leases. The earlier leases were re-examined and the Court noted that there was an obligation under those leases not to cause 'nuisance or injury'.

The Court appears to rely heavily on evidence from a former Mobil employee, who gave evidence that in the 1960s Mobil was risk averse and never considered spillage or contamination as acceptable practice.

The doctrine of waste was also re-examined by the Court. It determined that the High Court had applied the wrong test, and found that while oil storage was permitted, contamination was not authorised. Given the evidence of the former Mobil employee it determined that spillage and dewatering, which caused the contamination, was not normal or necessary for the permitted use of oil storage and the 'reasonable use' defence did not apply.

The Court found that as at 1985 Mobil was at legal risk of a potential claim as its neglect/practices had amounted to waste. In considering the 1985 lease in the context of that existing liability, it was not appropriate to read down the make good obligations to surface only.

Section 106 of the Property Law Act 1956 was excluded from the lease, which provided that regard had to be had to the condition of the premises at commencement. This suggested that the obligation to make good was not necessarily capped just to the standard of the (contaminated) leased site at commencement.

The 1985 lease was considered to be a 'stop-gap' measure in a longstanding and continuing relationship and the 1985 lease should not be read in isolation.

The Court of Appeal found that when entering into the 1985 leases, Mobil was at the negotiating table with actual or potential liability for its contamination. In light of this:

- The Court did not consider that it would be surprising for Mobil to accept responsibility to decontaminate, including in respect of contamination caused by other group companies, especially when it was Mobil that had caused much of the contamination itself; and
- The Court held that the clean and tidy repair wording required Mobil to deliver the land, including the sub-surface, in clean and tidy condition having regard to its condition in 1925. It noted that even if the express obligation under the lease (to leave the land clean and tidy) was not present, it would have implied the doctrine of waste into the lease to impose the same obligation on the lessee.

2016 Supreme Court

Mobil has now been granted leave to appeal the matter to the Supreme Court which should be set down for 2016. We await the next instalment of the dispute with interest. The two contrasting judgments to date illustrate that the outcome of litigation is never certain and reinforce the importance of getting the drafting of your leases right.

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PRACTICAL ASPECTS OF COOK ISLANDS RENT REVIEW ARBITRATIONS
IMPLICATIONS FOR NEW ZEALAND

Bob Hawkes

This is the second article in a three-part series by the author on the new Cook Island Arbitration Act 2014 and its implications for similar situations in New Zealand.

Arbitration process

The steps in the arbitration process are:

- The arbitrator has been chosen and appointed, with the appropriate terms of engagement agreement completed between the parties and arbitrator
- The arbitrator arranges a preliminary meeting with the parties, also usually attended by the party advocates, to discuss and confirm the way the arbitration will be conducted and to establish a procedural timetable. Meeting minutes usually follow for confirmation by all concerned and the meeting is often by teleconference. Submissions on the substantive dispute are precluded at this meeting
- The parties present submissions and evidence
- The hearing is conducted, if required
- The arbitrator considers the submissions and evidence and issues a decision – the award.

The period between the preliminary meeting and hearing might entail:

- A statement of claim by the claimant
- A response to the claim, or defence, by the respondent and this might include a counterclaim
- A reply to the response and response to any counterclaim by the claimant
- A reply to the response to the counterclaim by the respondent
- Requests for arbitrator orders
- Interrogatories
- An exchange of witness statements and collation of an agreed bundle of documents
- Opening statements by the parties.

All presented documents must be served on the opposing party(s) simultaneously with service on the arbitrator. Normally the arbitrator will read the material prior to the hearing to at least gain some understanding of the dispute issues. This is not a pre-judging of the matter, but merely a familiarisation of material to that point. A counterclaim does not normally arise in rent arbitrations.

Flexibility in process design is important, with an objective of avoiding unnecessary steps and arbitrator reading material. However, the rules of natural justice must remain paramount. The parties are free to settle the dispute at any time in the process, thus stemming the arbitration costs from that point. Such an agreement can be documented by the arbitrator issuing a consent award, if the parties so wish and the arbitrator agrees. It is the arbitrator's role to make a decision on presented submissions and evidence. It is the parties' role, supported by their witnesses, to present their case. A poorly presented case may result in a seemingly unfavourable award. It is the responsibility of expert witnesses to ensure at least their evidence is such as to create a full picture for the arbitrator.

Private discussions with the arbitral tribunal

The arbitrator is not available for private discussions, except in very rare circumstances of proceeding ex parte. This is a particularly important message for all. Difficult consequences can arise if the rule is broken, such as potential allegations the tribunal had private contact with a party or any other participant during the proceedings and thus breached the rules of natural justice, which might be potentially seen as biased. One potential outcome is the award being placed in jeopardy through court challenge.

In the event of a successful award challenge on these grounds it ultimately means wasted time and expense. Very succinctly, no individual or party representative has a right of sole access to the arbitral tribunal. There can be an exception when a party or the arbitrator may seek a quick answer on a process matter and that might be actioned more cost-effectively by a phone call. Such contacts must be limited to matters of the arbitration process and avoid any comments on the substantive issue of the dispute. The underlying reason is that the arbitrator is bound to treat each party equally and give the opposing party an opportunity to respond on any points made by a contender.

As a general rule there should be no phone calls to the arbitrator, except perhaps when they are initially contacted as to availability. Compliance with this rule saves embarrassment and awkward rebuffs.

Viva voce hearing

In the most structured form the viva voce hearing very much follows that of a typical court hearing:

- Claimant's opening statement
- Claimant's evidence in chief
- Cross-examination of the claimant's witnesses by the respondent at the end of each witness evidence in chief
- Re-examination of the claimant's witnesses by the claimant
- Any witness questions from the arbitrator
- Opportunity for the claimant and then the respondent to examine and then the claimant to re-examine solely on points raised by the arbitrator
- Respondent's opening statement

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- Respondent's evidence in chief
- Cross-examination of the respondent's witnesses by the claimant at the end of each witness evidence in chief
- Re-examination of the respondent's witnesses by the respondent
- Any witness questions from the arbitrator
- Opportunity for the respondent and then the claimant to examine and then the respondent to re-examine solely on points raised by the arbitrator
- Respondent closing
- Claimant closing.

The arbitrator may delay any witness questioning until completion of the respondent witnesses, otherwise there is a risk of being perceived as aiding a party's case by jumping in too early. On occasion it can be expected that the arbitrator may withhold questions until after the hearing and when deliberations towards award preparation are in hand. Such questions will be in writing, with each party given equal opportunity to answer. The claimant in the process steps is the party that activated arbitration, unless the parties agree otherwise, and usually it will be the landlord. It goes without saying that the respondent is the other involved party.

Hearing time can be reduced through agreement that all documents exchanged pre-hearing and then simultaneously served on the arbitrator be taken as read, leaving it for the various document authors to only highlight specific interest points during the hearing. The hearing style might vary from a rather formal type reflected above through to an informal meeting which adopts the basic format but in a relaxed style. Any process relaxation must not circumvent the natural justice rule, but ideally have an objective of limiting arbitration cost as much as practicable.

On the papers

In these days of electronic communication an arbitration can be very cost-effectively conducted on the papers. It saves hearing costs and the cost of tribunal travel and is a concept the modern Acts authorise. A rent review on the papers can simply entail:

- Arbitration agreement completion – the agreement should preferably include a simple statement of each party's stance and a process timetable in addition to the arbitrator's terms of engagement
- Claimant's written claim plus supporting evidence
- Respondent's written response plus supporting evidence
- Rebuttal of the respondent's input by the claimant
- Arbitrator desk-top deliberations on presented written material and issue of an award on the substantive matter, including an invitation for submissions on costs within a prescribed timeframe
- Arbitrator desk-top deliberations on costs submissions, if any, and issue of a final award.

A final award is avoided if the parties reach agreement as to costs. The second and third bullet points of the simple outline may be in parallel or sequential. If in parallel, then each party is given a rebuttal opportunity. Adoption of the process requires party/party agreement at the outset. Cost-effectiveness can be enhanced by the parties and their representatives resisting any temptation towards delaying tactics.

The process has its critics, particularly those who believe rent decision-makers should view the subject property and other properties cited for comparable rents. The criticism can be countered by well-documented evidence including digital photography, clear explicit pen pictures, aerial photography and maps.

Rent review arbitration in more detail

The rent review arbitration is fundamentally a consideration of relevant lease terms, coupled with economic and market transaction evidence to derive a rent in terms of the given lease. The ideal is to concentrate on comparing like with like. It can be expected a valuer will refer to transactions bearing on the value deliberations as either comparables or market evidence, or both. If land is at issue, then focus on other land rents as comparables. If it is a building, then focus on building rents as comparables.

The Cook Islands is a relatively small market by international standards. However with a relatively small volume of real estate market transactions at any given time, if any, the skilled valuer can be expected to work within those parameters to arrive at a suitable assessment.

The New Zealand land ownership system is such that measurable ratios of values and rents between land and improvements can be gained from a variety of transaction data. This experience might well be adapted for arriving at an assessment within the Cook Islands.

The rent assessment basis

Invariably leases prescribe that the rent at review is to be market rent or current market rent as at the review date. Note that there are Cook Islands ground lease exceptions which prescribe the rent to be a percentage of, for instance, land value. A substantial portion of the discussion from this point highlights

> *In these days of electronic communication an arbitration can be very cost-effectively conducted on the papers.*

The classical rent assessment involves analysing existing market rents and then applying the result on a square metre, or perhaps per hectare, rate to derive the subject assessment.

matters likely to arise in evidence. There is no intention to skill lawyers as valuers, but to merely flag potential points for consideration in case presentation.

Market rent

A web search indicates wide usage of the term 'market rent'. There may be variations in interpretation but most, if not all, are relatively similar. An alternative is fair market rent. It can raise idiosyncrasies and each example needs to be regarded on its particular merits. An interpretation of current market rent is noted at [11] of the Cook Islands High Court judgment *Mil Properties (Cook Islands) Limited formerly known as Standard Chartered Property (Cook Islands) Ltd v The Landowners – Enuakura Sec 205A No. 1, Avarua*, Savage J, High Court of the Cook Islands (Land Division), 8/7/2010, Application No. 375/2009: '...what a reasonable, wise and willing tenant would be prepared to pay and what a landlord with those attributes would be expected to obtain...'

The International Valuations Standards Council 2013 definition is:

> **Market rent** – the estimated amount for which an interest in real property should be leased on the valuation date between a willing lessor and a willing lessee on appropriate lease terms in an arm's length transaction, after proper marketing wherein the parties have each acted knowledgeably, prudently and without compulsion.

A somewhat similar concept applies in the definition for market value:

> **Market value** – the estimated amount for which an asset or liability should exchange on the valuation date between a willing buyer and a willing seller in an arm's-length transaction, after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion.

Fair value is defined as:

> **Fair value** – the estimated price for the transfer of an asset or liability between identified knowledgeable and willing parties that reflects the respective interests of those parties.

This is not to be confused with fair value as applied to financial reporting. There is no 2013 Standards definition for fair rent. The definitions form part of generally accepted valuation principles fundamental to and underpinning the valuation discipline internationally and are adopted by the Australian and New Zealand property professional institutes.

The established valuation principle of fair rent has been discussed in the New Zealand courts in cases such as *Granadilla Ltd v Berben* (1999) 4 NZ ConvC 192,963, 10/3/99, Blanchard J, Court of Appeal (Richardson P, Blanchard and Salmon JJ) CA191/98, in considering a challenge on points of law against an umpire's ground rent review award. The judgment discusses the prudent lessee test and compares it with the willing lessor/willing lessee approach. The umpire had adopted a prudent lessee test. The court was not persuaded the umpire had erred, noting: '... the fair rent is what the lessor can reasonably expect to be offered, not what the lessor would like to receive.'

The prudent lessee test is subsequently discussed in *Casata Limited v General Distributors Limited* [2005] 3 NZLR 156, 13/4/2005, Court of Appeal (Glazebrook and Hammond JJ, with Chambers J dissenting in part) CA84/04, and in *Sextant Holdings Limited v New Zealand Railways Corporation* [1993] 2 NZ ConvC [95-201], 19/3/93, Tipping J, Court of Appeal (Richardson, McKay and Tipping J) CA71/92. In *Sextant* the judgment compares the prudent lessee concept with the willing buyer/willing seller alternative, concluding there is no significant difference. Citing from (78) of *Casata*:

> It is true that the arbitral tribunal referred to the prudent lessee test as set out in the *Wellington City* case ... It, however, stated, citing *Sextant Holdings*, that there was no discernible difference between that test and the willing lessor/willing lessee test articulated in *Sextant Holdings*. It then later in the award ... clearly articulated the willing lessee test as assuming that the rent determined will be the maximum sum a lessee will pay and the least amount that an informed lessor will willingly accept, effectively the test in *Sextant Holdings*, which Mr Hodder accepts accords with ... the parties' agreement. This was after the tribunal had quoted from *Granadilla* and shows that it saw no retreat from *Sextant Holdings* in that decision. Neither do we.

Rent assessment approaches for land

Two approaches found in New Zealand are classical and traditional. The classical approach is that involving a direct comparison with appropriate established rents. The traditional approach involves assessing the land value and then applying a percentage return factor or rate of return to derive the assessed rent. The attributes of the two are discussed in the New Zealand courts. An example is at [43] and [44] of *Casata*, where Counsel for *Casata* describes both methods.

Classical assessment approach

The classical rent assessment involves analysing existing market rents and then applying the result on a square metre, or perhaps per hectare, rate to derive the subject assessment. The analysis involves adjustments for site differences and peculiarities between the cited comparable transactions. This approach has inherent difficulties when there is a short supply of open market leasings, or even possibly none.

The traditional rent assessment involves analysing market land sales to assess a land value for the subject, then applying a rate of return to calculate the related rent.

A shortage of transactions can be a problem for larger markets as well as the small. See, for instance, the comment in a New Zealand context at [80] of *Casata*. The main problem is an arbitral award challenge, with the lack of direct market comparables apparently playing only a relatively small part in the court deliberations. The case concerns a ground rent arbitration for Wellington suburban commercial land. The valuer faced with such a dilemma will weigh other data, including possibly transactional and economic, to derive an answer.

Traditional assessment approach

The traditional rent assessment involves analysing market land sales to assess a land value for the subject, then applying a rate of return to calculate the related rent. As with the rent analysis of the classical approach, an analysis involves adjustments for site differences and peculiarities between the cited comparable transactions, but from a land sale perspective rather than leasing. The appropriate percentage return to apply in deriving the rent also involves analysis and the valuer's judgement from the likes of:

- Analysing the return reflected by land sales where approximate and simultaneous sale and ground leasings have taken place and a rate of return is identifiable
- Adopting the return from, for instance, gilt-edged securities and applying margins or reductions for any perceived added risks or alternatively better security when comparing the investment types.

This approach is likely to be very problematic for the Cook Islands through the land tenure producing no land sales and therefore no fundamental valuation baseline. Some assistance might be gained by sourcing transactions from other states and applying suitable adjustments to derive Cook Islands values. This approach can be considered problematic, as it entails value judgement calls that could be conceivably difficult to justify on account of no Cook Islands land sales for referencing. That in turn can result in wide discrepancies between valuer assessments.

Rent assessment approach for improvements

The assessment approach for buildings and other improvements is normally the classical approach outlined above.

Evidence – comparing rents

There are a number of factors the professional considers in comparing existing rents for a rent assessment task. These should ideally receive serious consideration in the rent dispute arbitration. It is primarily the responsibility of the parties to source and table the information. It is not the arbitrator's responsibility to search for it. Examples of more detailed factors likely to be encountered in rent analysis under land and building categories are now outlined in more detail. At least some pertinent factors can be gleaned from Cook Islands court judgments such as:

- Adjustments for timing between rent reviews such as five-year as against 10-year reviews
- Adjustments for site frontage differences
- Allowances for tenant improvements
- Adjustments for site area differences
- Adjustments for time difference fluctuations between the subject effective date and the effective date for cited comparables.

Other required adjustments might include:

- Differing lease terms, discussed in more detail in the third article in this series
- Differing land use types, for instance, residential, commercial, industrial, tourism or rural
- Property location
- Surrounding environment
- Site contour
- Site aspect
- Ground quality including foundation strength or excavation difficulties
- Property use such as retail, office, warehouse or factory
- Building type
- Building construction
- Quality of construction
- Building age and obsolescence
- Building floor area
- Internal stud height
- Use of yard space and types of paving
- Building aspect
- Full details of tenant fitout
- Identification of 'key money' either for the business or for the leasehold interest, or both
- Any goodwill payments to achieve a transaction
- Clarification of improvements ownership.

It is important to make sure all referenced buildings are measured on the same basis. If the gross area basis is adopted then ensure all cited comparables are also measured around that parameter. Conversely, if the net measure basis is adopted then they all need to be on that basis. Also ensure all floors are measured.

Final article

The third and final article to be published in the next issue of this magazine concludes the discussion on the evidence and arbitration process.

GREG BALL

Greg Ball's been President of the Property Institute since mid-2015, when he was elected by the Board at the Christchurch Annual Conference with a remit to leading the Institute through a time of intensive change and improvement.

Based in Wellington, Greg has become almost synonymous with The Property Group (TPG), a company formed as a state-owned enterprise property consultancy in 1996 under the original name of Terralink Property Services. In 1999, Greg led a management buy out of the firm and took it private alongside a core team of 13 colleagues under its current name. Today, TPG employs over 130 staff, spread throughout the country across 12 different offices.

From its inception, TPG's activities focused on the New Zealand Transport Agency (NZTA) and the Public Works Act. To this day the NZTA remains a key client for them, and they are the single largest group of LINZ accredited suppliers. Their activities have widened significantly over time though, and they've been recently involved in projects ranging from Telecom's XT Network, the Christchurch Red Zone, Chorus rolling out commercial fibre, and plenty more.

Greg specialises in long-term strategic planning and change management – skills the Institute needs more than ever during this period of intensive change. Even within his first year as President, Greg's made his mark on the Institute with a focus on improving the quality and professionalism, both of the services it offers and its internal operations.

During his time as a member of the Property Institute, Greg's achieved a number of accolades, including:

- Gaining registration as a Property Consultant and Property Manager
- In 2008, receiving the Property Institute Industry Award for an individual demonstrating outstanding achievement and vision, and contributing positively to the property sector
- In 2015, receiving a fellowship of the Institute.

More recently, Greg stepped back from his involvement in TPG, appointing a new management team in 2012 and moving aside as Managing Director – to focus on succession planning and the long-term viability of the business, an aspect often overlooked in the property industry. He remains involved in the firm as Executive Director, and lately has been spending a significant amount of time based in Christchurch working alongside the Canterbury Earthquake Recovery Authority on the rebuild of the city.

Greg's term as President lasts two years, and come mid-2017 when this expires, the Institute he hands on to the next President is likely to be a very different body to the one he inherited.

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