

Christchurch - The complexities of compulsory acquisition

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Shortly before the Canterbury Earthquake Recovery Act 2011 (**Act**) was passed, the Earthquake Recovery Minister, Gerry Brownlee, said that the power of the Christchurch Earthquake Recovery Authority (**CERA**) to compulsorily acquire private property under the Act will be used sparingly. He confirmed however that the power would be important for the recovery of the Christchurch suburbs as well as the Christchurch CBD.¹

There has been a significant amount of commentary regarding CERA's powers to demolish or take control of dangerous and/or earthquake prone buildings. There has been markedly less comment with respect to how and where CERA may use its powers of compulsory acquisition and the disputes that are likely to arise in respect of the 'current market value' of compulsorily acquired land. This may be because CERA and the Christchurch City Council are still considering whether some suburbs should be rebuilt at all and where the Christchurch CBD will ultimately be based.

This newsletter examines the power of CERA to compulsorily acquire land, the acquisition process and some of the key issues which are likely to arise. Our comments provide a broad overview only. Further issues relating to matters such as valuation, insurance and security interests, some of them complex, are likely to arise and will require substantial further analysis.

Power of compulsory acquisition – purpose and objection rights

The Minister and the Chief Executive of CERA have extensive powers under section 53(4) of the Act, including the power to acquire or dispose of property and to compulsorily acquire land. The Minister starts the process by giving a Gazette notice declaring that the land is to be taken in the name of the Crown.

The Act is silent as to the purpose for which the Minister may compulsorily acquire land. Media commentary suggests that the power may be used for building new commercial centres and implementing other redevelopment plans; but this is not a stated purpose under the Act.

The Minister must of course exercise powers in accordance with the general purposes of the Act, including:

- providing appropriate measures to ensure that greater Christchurch and the councils and their communities respond to, and recover from, the impacts of the earthquakes;
- enabling a focused, timely, and expedited recovery;

¹ 12 April 2011 671 New Zealand Parliamentary Debates 17898

- facilitating, coordinating, and directing the planning, rebuilding, and recovery of affected communities, including the repair and rebuilding of land, infrastructure, and other property; and
- restoring the social, economic, cultural, and environmental well being of greater Christchurch communities.

Apart from these very general statements, there is no other guidance which the Minister or CERA must follow when exercising their compulsory acquisition and disposal powers of private land.

Can landowners object to the exercise of these powers?

Unlike the Public Works Act 1981 (PWA), there is no statutory right to object to the decision to compulsorily acquire land under the Act.

However land owners are entitled to seek judicial review of the exercise of the Minister's power on the basis that he is not acting in accordance with the purpose of the Act.

It is understandable and pragmatic that the powers given to CERA and the Minister are available within a widely drafted framework to allow for many unforeseen issues which they will have to deal with, including, for example, the size and location of ongoing aftershocks and how these will affect town planning.

The six process steps of compulsory acquisition

Once the Minister determines that land is to be acquired, the six process steps are:

1. The Minister publishes a Notice of Intention to take the land in the Gazette, which must be publically notified twice in the local newspaper. The Notice must identify the land (address or other description) and describe the purpose for which the land is to be used.

Given the comments above on the lack of specific purposes in the Act, the specified purpose in the Notice will be important for landowners who may wish to challenge the acquisition;
2. The Minister must also serve the Notice on the landowner and registered mortgagee (and others with a registered interest in the land), unless it is impracticable to do so;

3. The Notice must be lodged with the Registrar General of Land, who will register it on the landowner's title;
4. The Minister may then recommend that the Governor General make a proclamation declaring that the land be taken in the name of the Crown;
5. The proclamation must then be published in the Gazette and publically notified within one month, presumably in the local newspaper's Public Notices section; and
6. The land is then deemed to be vested in the Crown on the fourteenth day after the proclamation is published in the Gazette.

The Crown receives the land free from all encumbrances, which would include the discharge of registered mortgages and other registered security interests. The Crown also inherits the landowner's rights against the landowner's insurance company for payments relating to the land, buildings or other property on the land.

If the landowner (or its tenant) does not give vacant possession of the land within one month after the proclamation has been published in the Gazette, the Minister may seek an order from the High Court directing the owner or occupier to give vacant possession. The implications for tenanted properties and liabilities and rights as between the landowner and the tenant should be carefully considered.

Compensation – determining the actual loss and the claims process

Compensation for compulsorily acquired land is determined as at the date of the compulsory acquisition². In other words, the appropriate amount of compensation is determined at post earthquake value.

The Honourable Gerry Brownlee has commented that powers to forcibly acquire land are a 'backstop' if commercial negotiations fail, which then cause unacceptable delays to the recovery. He stated: *"It is if commercial negotiations fail and other people are prevented from getting on with the bigger recovery. Paying post quake market value for property is a fair measure because, if commercial negotiations fail, there is no other value for the property."*³

² Presumably this will be on the date that the land becomes vested in the Crown. Pursuant to section 55(6) of the Act, this will be on the 14th day after the day on which the proclamation was published in the Gazette.

³ Ben Heather, Landowners may be forced to sell at loss, *The Press*, (New Zealand, 19 May 2011)

What losses can landowners claim? The Act limits what losses landowners can claim as compensation. Compensation is defined as **actual** loss. Landowners cannot claim for economic or consequential loss, business interruption or any part of a loss that ought reasonably to have been insured. Landowners cannot claim any other loss that the Minister reasonably considers is unwarranted and unjustified. These are just some of the ten exceptions specified in section 61 of the Act.

What is the process for lodging claims? The procedure for claiming compensation is set out in sections 60 to 67 of the Act and can be summarised as follows:

- The landowner must file a properly completed claim for compensation with CERA on a specific claim form within two years after the exercise of the acquisition power.
- The Minister then determines whether compensation is payable, and if so, the amount of the compensation. The Minister must take account of the property's market value as at the date of the compulsory acquisition, as determined by a registered valuer. The Minister must also consider the relevant provisions in Part 5 of the PWA (see Issues section below for a more detailed discussion of what these are).

Landowners have to be given a reasonable opportunity to make representations as to the nature of the claim and the amount of compensation payable.

If the landowner is dissatisfied with the level of compensation payable, they can appeal to the High Court within ten days of the determination.

At the appeal, the High Court may appoint one or more suitably qualified persons to assist in giving advice as to the value of the property. The Court may give as much or as little weight to this as it wishes.

Issues to consider – ‘current market value’, the position of insurers and refinancing issues

The acquisition and compensation processes under the Act raise many issues which require careful consideration. These include the measure of ‘current market value’ and implications for insurers and mortgagees.

Current market value

Valuation issues in Christchurch will be vexed. In this section, we provide a broad overview of the measure of ‘current market value’ under the Act. At present, there are more questions than answers with respect to how this is likely to work in practice.

As stated above, the Minister determines compensation with regard to the current market value of the land as determined by a registered valuer and, so far as practicable, in accordance with Part 5 of the PWA.

What are the valuation factors under part 5 of the PWA?

Briefly, no allowance is to be made due to the fact that the taking of the land was compulsory. Further, the value of the land is to be taken to be that amount which the land **if sold on an open market by a willing seller to a willing buyer on a specified date** might be expected to realise.

The Minister and/or the High Court will most likely refer to decisions under section 62 of the PWA in considering claims for compensation under the Act. As many claims under section 62 are resolved in private negotiation or arbitration, recent judicial commentary is limited.

A key case⁴ has confirmed that the value as at the date of acquisition is affected by the condition of the property as at that date and “*The value was necessarily affected by all the advantages which the land possessed and these might be a matter of future or even contingent enjoyment*”.

This ‘current market value’ test is likely to present difficulties, particularly as the factors which are relevant to the assessment of these ‘advantages’ are uncertain.

Consider the following factors:

- **Zoning changes** - Until CERA and the councils have created and publicly released the rebuild plan for Christchurch, this will remain unclear. A property's value must be determined as at the date of acquisition and zoning in place at that time will be the relevant measure. If the zoning changes between the date of the earthquake(s) and the date of acquisition, and this causes a significant decrease in value, landowners cannot claim that decrease as actual loss. But what if the zoning hasn't changed on the date of acquisition, but is likely to change - is this a factor to value the ‘potentiality’ of the land?

⁴ *Tauhara Properties Ltd v Minister of Works and Development* [1980] 2 NZLR 673 at page 677 - this case concerned land acquired under the Public Works Act 1928. The Court cited commentary on value from *Turner v Minister of Public Instruction* (1956) 95 CLR 245

- **Proximity to the CBD and key services** - Where will the CBD be located in the future? As a property is to be valued at the time of acquisition, will valuers be required to assume that the CBD is in its current position, or will 'CBD' acquire a new meaning as businesses relocate to premises around Christchurch?
- **Development potential of the land** - Recent commentary suggests that the current market preference in Christchurch is for low rise, pedestrian style office blocks. How will this affect the development potential of the acquired land?
- **Geotechnical issues will be important** - Earthquake analysis and geographic surveys identifying new fault lines are likely to be a relevant consideration.

The High Court appeal procedure may become the forum in which market perceptions and expectations as to market value and its defining factors are considered in detail. The market is constantly changing and is also sensitive to factors such as environment (for example ongoing aftershocks) and time. Two blocks of land that are acquired six months apart may be determined to have very different 'current market values'.

Insurance and refinancing issues

Compulsory acquisitions under the Act that give rise to valuation issues, or even the potential for such acquisitions, are likely to have negative consequences for insured landowners and other interested parties such as banks and other lenders.

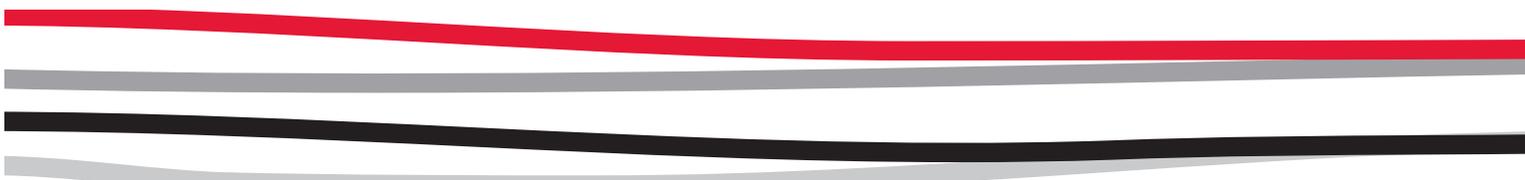
Important insurance issues include the following:

- Insurance policies normally provide cover for the replacement value of buildings only where the landowner in fact replaces them on the same site and within a reasonable time. Otherwise, only indemnity value (which may be a much lower amount) is payable. Where a landowner's land is compulsorily acquired, an insurer may not necessarily accept the purchase of a replacement site and building elsewhere or the erection of a new building on another site, particularly where there has been a lengthy delay.
- Insurance policies normally indemnify property owners for physical loss and damage to land (which in the case of residential land is covered primarily by the Earthquake Commission) and buildings. They do not normally provide cover for loss of value that arises as a result of changed market perceptions. Many landowners are likely to find that the physical repair costs to their land and buildings are significantly less than the devaluation losses they have suffered because their land and buildings have become undesirable. The devaluation may occur as a result of increased public recognition of their susceptibility to earthquake damage or decisions by other landowners or CERA's decision not to rebuild in their area. These devaluation losses are not usually covered by insurance companies.
- Landowners whose land is compulsorily acquired will not normally be insured for losses they suffer because their entitlement to compensation under the Act (which is assessed net of any entitlement to insurance proceeds) is significantly less than the pre-earthquake value of their land and buildings.

As a result, landowners may also find that the insurance amount is not enough to repay their mortgage monies to lenders who have financed properties on the basis of their pre-earthquake values. This in turn may prevent landowners from finding additional mortgage funds to reinstate land or buildings damaged by the earthquakes. If lenders rely on their contractual entitlements under loan agreements and insurance policies to receive the proceeds of insurance directly in repayment of their loans, the landowners will still suffer a repayment shortfall.

Conclusion

The widely drafted purpose of the Act is clearly necessary for the rebuild and restoration of Christchurch, and the consequential wide powers of compulsory acquisition are arguably necessary to achieve this purpose. It remains to be seen however how the compulsory acquisition process under the Act will work in practice and how the issues highlighted above will be addressed.



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