REVIEW OF VALUATION CASES

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1. CHERMSIDE SHOPPING CENTRE

Eleven major regional shopping centres appealed against very substantial increases in their statutory valuations (relevant date 01/10/2002). Because of the valuation approach adopted by the State and the resultant extensive expert evidence adduced, two of these appeals effectively became test cases for the others involved. *Chermside* and *Pacific Fair* were these two.

The statutory valuation (after objection) for *Chermside* was $54,000,000 although the respondent chief executive contended at hearing for a final figure of $151,000,000 or $142,500,000 (depending on a question of law). The appellant's estimate was $21,500,000. This was the figure that applied as at 1 October 2001.

Although *Chermside* and *Pacific Fair* were heard together, separate decisions were delivered. Many of the common issues were considered in the Chermside decision with additional issues, specific to *Pacific Fair*, discussed in the latter decision (noted below).

The two cases were exhaustively presented over some 50 days of evidence with 27 witnesses called to give evidence. The *Chermside* decision runs to some 242 pages. Many interlocutory issues came before the Court prior to commencement to the full hearing.

Chermside was described as a "major regional shopping centre", developed in stages since 1957. It was the first regional shopping centre constructed in Australia. Use as a regional shopping centre was consistent with the prevailing planning regime.

The key issue in both cases was whether a valuation determined under s.3(1)(b) *VLA* (the primary method) was exceeded by one determined under s.3(2) (the subtraction method). The primary method essentially involved the analysis and application of comparable sales (purchased mainly for redevelopment). The more complex and less conventional subtraction method involved the initial determination of an improved value and then deducting from that the value of improvements.

Improvements included not only physical improvements (including site improvements) but also (as a result of the 2003 *VLA* amendments) intangible improvements. The latter included items such as the value of leases and goodwill. Whether intangible improvements should be deducted in a s.3(1)(b) approach as well as a s.3(2) was a key issue before the Court.

The Court initially determined a figure under s.3(1)(b) for Chermside based on two sales. The first was a subject sale in December 1996 prior to its redevelopment with an appropriate allowance for retained improvements. This was considered the best evidence of value. The second sale was of the Burwood Shopping Centre (in Sydney's inner west) in 1992, the sale of a dated existing centre essentially for redevelopment. The dated sale figure could not be adjusted but was used as support for a 1997 valuation and a serious investment decision by the purchaser's Board based on that valuation. It was this 1997 valuation that was relied on. Other tendered sales were rejected as not really comparable, considering the size of the subject.

On this basis, the unimproved capital value of $112,000,000 was determined for Chermside under s.3(1)(b).

Given the evidence led at the hearing, the Court was then required to perform a valuation under s.3(2). After some adjustments to parties figures, an improved value for Chermside was arrived at, basically by the process of capitalisation of net annual income. The contentious areas were the value of the physical improvements and, more so, the value of intangibles (there was a statutory cap imposed by legislation on what the latter could be – 20% of the improved value).

The Court stressed it was not required to precisely calculate the unimproved capital value under s.3(2) if there was sufficient evidence that it was likely to be a lesser figure than s.3(1)(b) determined figure. It thus performed what it referred to as a "rational" (shortened) approach to s.3(2) – concluding that any derived unimproved valuation would necessarily arrive at a figure less than that determined under s.3(1)(b).

It thus followed that the s.3(1)(b) figures prevailed. As there were acceptable sales evidence, the Court expressed much greater confidence in a determination based on this source as opposed to the subtraction method.

In the process of determining the appeal, the Court addressed a wide range of issues, the principal ones of which are noted in brief summary below:

1. Section 3(1)(b) Approach

- Under this provision, unimproved value was to be based on the "fee simple" of the land. Such required disregarding any restrictions on title or user other than those imposed by general law. Thus, any leases which encumbered the title were to be disregarded.

- It was necessary to determine "highest and best use" of the subject. That involved the question of whether the expression assuming "the improvements did not exist" meant that "assuming the improvements had never been made". It was held that it did not. The term contained a temporal aspect, requiring consideration of the situation at the time the valuation was to be made. Benefits that notionally removed improvements bought to the land at the valuation date were to be considered. Section 3(1)(b) required that the effect the improvements had on the land prior to the moment of valuation was relevant to the value of the land. What was not relevant was the enhancement in value which the improvements added at the moment of valuation.

  The formulation developed in the High Court decision of *Nathan* (1915) – [*The Albion Park Racecourse* case] was adopted in preference to the approach of the Privy Council in *Toohey's* case (1925). A lengthy analysis of the history of these cases was undertaken by the Court.

- The highest and best use of the appeal land was a regional shopping centre, developed to a standard that would have been sought at the relevant date by a prudent developer. Such use was proved by the history of the centre. It was

not speculative. Agreements for lease (AFL's) in place confirmed this highest and best use.

- The approach to valuation under s.3(1)(b) was not altered by the 2003 amendments. There was no need under s.3(1)(b) to consider improved value or any intangible improvements which are part of that value.

- Under either a s.3(1)b) or s.3(2) valuation, it was first necessary to determine whether the structures on the land were "improvements". The *QNI* decision provided the appropriate test. The complex *QNI* principle is well analysed in this Court decision. The test under *QNI* is one of ascertaining whether the value of the land with structures in place is higher than the value for any alternative use which, to be effective, would involve the cost of demolishing and disposing of the structures. If the value with the structures is higher, then the structures add value and are improvements. If the alternative use value together with a cost of demolition is higher, the structures add no value and therefore are not improvements.

  A useful illustration of the application of *QNI* is provided in paragraph [135] of this Chermside decision.

- As there was a national market for shopping centres, it was permissible to use interstate sales evidence. Locational differences in values were an important consideration in valuations and must be addressed. However, a locational difference did not, by itself, operate to exclude a particular property from consideration.

- No allowance for development approval (DA), including time for achieving such, was to be made in arriving at an unimproved value under s.3(1)(b) in analysing a sale property.

  A different position applied with respect to s.3(2) where s.4 requires the inclusion of all improvements in settling the improved value under that provision.

- Valuation methods such as a calibration method or an allocation method involved fairly precise mathematical calculations and comparisons. Such could be used to support rather than supplant more traditional comparative methods were a wider range of items involving value judgments were employed. The former methods could not take into account, however, such matters as locational differences, particular features such as cost differences and any latent potential in the land.

- Certain valuation approaches adopted by the American Appraisal Institute were considered valid for local application.

- In using the Chermside 1996 sale for redevelopment to arrive at a comparable figure for the property the subject for valuation, two factors required adjustment to be made. First, the need to develop the land as purchased with retained structures and tenancies in place was a <u>disadvantage</u> to the sale land in

comparison with the subject land treated as having a clean slate from which development of a regional shopping centre could take place. Second, the redeveloped shopping centre on the sale land had to accommodate the Myer store in a design sub-optimal to one that could have been chosen had the shopping centre been developed on a bare site.

- It was not proper for valuers to rely on hearsay evidence where evidence was not reliable, was important, was not an admission against interest and was not a matter of fact, but opinion. However, the task of a valuer would be unduly compromised if hearsay evidence was not generally received. Where it was admissible it was not accorded the same weight as direct evidence.

- In a sales analysis of a completed project, it was not proper to make an allowance for contingencies in attempting to value site improvements. As the project was completed, the costs are then known.

- The principle in *Executor Trustee* case requires doubts in rating and taxing cases to be resolved in favour of the landowner. However, this applied only to the final determination stage and not with intermediate steps (e.g. the selection of an appropriate capitalisation rate in calculating the improved value from net rentals).

2. Section 3(2) Approach

- The calculation of unimproved value by the s.3(2) method involved three steps. First, the improved value of the land has to be ascertained. Second, the value of improvements is estimated and, in the third step, that estimate is deducted from the improved value to produce the unimproved value figure.
  It is quite possible for a valuation under s.3(2) to be not only based on a different use from that under s.3(1)(b) but for a substantially different value to result.

- Under the 2003 *VLA* amendments (s.35(A)) the appellants are required to provide the chief executive with details of intangibles to ensure that they are considered in calculations; (the appellant had lodged the necessary application here, alleging the value of intangible improvements was $75,500,000).

- A s.3(2) exercise is not carried out on the basis that the characteristics of the land are being valued. The resultant unimproved value figure is the product of a calculation. However, care needs to be taken that there is not included in the value of intangible improvements (including goodwill) any element of value that is properly attributable to land and therefore ought not to be considered part of goodwill. The quasi-monopoly opportunity engendered by the Town Planning classification of the land for a regional shopping centre cannot form part of the relevant goodwill.

- For an item to be classed as non-physical or intangible (and thus deducted as an improvement) under the 2003 amendments, it must provide a benefit to the land; it must enhance land value, but such benefit is not confined to above market (rental) values.

Benefits of leases would include

- The securing of rental income, therefore the disposal of development risk;
- The saving and legal survey and agency costs of establishing those leases;
- No delay in settling lease terms;
- Avoidance of non-receipt of revenue for the period leading up to the occupation by the various tenants;
- Above market rent;
- No uncertainty as to the actual tenants who would be secured.

- The Court stated that in the construction of s.3(2), it could not attribute to Parliament any intention that the section (which is a proviso) be relied on to generate an unimproved value substantially greater than could be obtained by the more reliable and traditional approach under s.3(1)(b). Intangibles had to be considered in a different way to that propounded by the respondent – the latter's approach resulted in only a minimal value being attached to such items.

- A development approval (DA) was a non-physical improvement which generated a substantial benefit in that it allowed the occupation of the building by tenants, the consequent use of the land as a shopping centre and the generation of income for the landholder. However, a DA was not a statutory right merely given, but was a right whose form and content were moulded by what the applicant developer contributed to the process. It was therefore, in terms of s.6(5) *VLA*, an intangible improvement and fell to be valued as part of the improvements of the subject land. Different considerations applied from those under a sale analysis approach under s.3(1)(b).

3. Goodwill

- "Goodwill" was not defined by the legislation but, for the purpose of s.6(5), is a non-physical improvement which provided benefit which is of value to the land including the physical improvements. Such benefit forms part of the improved value of the land. The Court adopted evidence of one of the appellant's witnesses in indicating what factors contribute to the goodwill of an established shopping centre. Items nominated were:

  - Trading history of the centre
  - Customer loyalty in shopping preferences;
  - Market recognition;
  - Brands strength;
  - Competitive advantages;
  - Tenant mix.

Expressed at its simplest level, goodwill was calculated as the difference between the value of the entity as a whole and the value of the NTA (net tangible assets).

- Goodwill was not severable from the enterprise conducted on the land. It could not exist in gross. To include goodwill as part of the market value of the fee simple for the highest and best use of a regional shopping centre was not to

value the fee simple in the manner explained in the *Brisbane City Council v Valuer-General*.

4. Value of Improvements – Difficulties

- Difficulties in valuing improvements, particularly on highly improved properties have long been recognised by the Courts. Typical problems are with invisible improvements, cost of effecting improvements and varying depreciation rates. Allowance for escalation of construction costs is a further difficultly. The difficulties are magnified by the need to value intangible improvements. The summation (or piece-meal) method of valuation has not been widely accepted by valuation courts; it is really a method of last resort. The above points are illustrated by the difference between the appellant's estimate of physical improvements and that of the respondent – a difference of some $67,000,000.

5. Rational Method

- In carrying out a "rational" (shortened) s.3(2) approach, the Court started with its calculated improved value then deducted the respondent's (adjusted) valuation of tangible improvements, including holding costs, and then its s.3(1)(b) determined unimproved value. It thus arrived at a <u>minimum</u> value of intangible improvements. Under this process, it reasoned that any unimproved land value <u>fully</u> calculated under this process would have been less than the $112,000,000 determined under s.3(1)(b). As a s.3(2) exercise sets the minimum figure under the VLA, it followed that the $112,000,000 calculated under s.3(1)(b) should stand.

6. Relativity

- The desire for relativity in applied unimproved statutory values for similar properties were stressed by the Court. Concern was expressed if different valuation approaches – one more generous for land owners who settled their objections and another for those who proceeded to appeal – for similar properties revealed different final results.

7. Principles for a Taxation System

- Key principles for any proper Taxation System were considered to include simplicity, efficiency and equity.

  Section 3(2) was not considered to exhibit simplicity or lead to an unimproved capital value as that concept was generally understood. It was further complicated by the need to take intangibles into consideration. Also the level and length of litigation impinged on efficiency. A factor in an equitable system was the need to have correct relativity in values.

  However, the Court considered that it was ultimately for Parliament to consider the application of these elements in any valuation system.

2. PACIFIC FAIR

This case was heard in conjunction with the Chermside Shopping Centre appeal but separate decisions have been issued in each case. The Chermside decision (noted above) covered many of the broader issues common to the two cases. A number of the important issues more related to Pacific Fair are noted here.

Pacific Fair is a "super regional" shopping centre at Broadbeach on the Gold Coast. It opened in 1977 and has been progressively enlarged. The site was originally filled with sand accessed from Little Tallebudgera Creek.

Both parties tendered valuation evidence directed to both a s.3(1)(b) approach – the "primary" method – and s.3(2) approach – the "deduction" method.

s.3(1)(b) Approach

In the *Chermside* case, the Court, after considering a range of sales, had evidence, had settled on a site improved valuation of $132,988,000. It then compared the Chermside site improved value to Pacific Fair to arrive at a site improved value for the latter. (Basically a s.3(1)(b) approach.)

From this site improved figure of $165,000,000 the site improvements had to be assessed and deducted. A figure of $128,200,000 was arrived at under this approach.

Site improvements (Fill Source)

The fill placed on the subject land when it was originally developed had been dredged from alluvial deposits in a nearby waterway and pumped onto the land. The respondent proposed that method as the basis for the estimation of cost and time delay for effecting the required fill. The appellant proposed that the fill would need to be trucked to the site from an outside source. Its position was there was little prospect of the dredging method being permitted at the relevant date (2002).

The court held that the estimated amount reasonably involved in obtaining fill should be based on sources available at the relevant date for valuation.

There was evidence that it still may have been possible to use fill dredged from nearby water courses (for at least part of the material necessary) but subject to a range of extensive and time-consuming approvals. However, there was no guarantee such approvals would eventually have been forthcoming – that is, the risk factor had to be included in any calculation of this source.

The difference in cost between the dredged fill and the truck fill was such that, even without the cost of studies being taken into account, the prudent developer would not have elected to pursue access to alluvial fill unless the prospect of accessing the total amount available by dredging was substantially without risk. The Court concluded that that not the case.

Ultimately, the Court decided on a cost per metre based on supplying trucked fill to the site.

s.3(2) Considerations

In analysing the respective approaches by the parties under a s.3(2) "deduction" approach, the Court addressed a number of important issues. It was confident that an acceptable improved value could be determined on the evidence presented. However, it was the assessment of the subsequent deductions that caused concern.

1. Cost of building structures on the subject land.

In the quantity surveying estimates of the appellant, figures based on the estimated new replacement cost (ENRC) of the existing structure were provided. The Court held this to be a notional substitution of structures. However, it was clear under the VLA that the improvements required to be valued were to be the improvements that were on the subject land.

The court held the correct approach was to identify the improvements to be costed and then assess what would it cost to effect them at the relevant date. If because of the antiquity of the item it would not be replicated at the relevant date, then alternative forms of structure could then be considered. If a more expensive method of filling, for example, than the original needed to be employed, costing should be on the basis of the more expensive method; alternatively, if a less expensive modern construction method would be used today, then that should be costed as long as the result was equivalent to that now existing.

Different improvements from those in place should not be costed if, for example, they were aesthetically more acceptable or provided a more secure or stronger structure, unless their inclusion was justified from reasons discussed above.

Rather than use the "as constructed" plans on the subject building which were available to the appellant, the appellant's quantity surveyor provided evidence of a conceptual shopping centre, having a floor area which approximated that of the subject property. The respondent did not produce any evidence of as constructed plans either – but merely audited the quantity surveying evidence of the appellant. He perhaps could have subpoenaed (or sought other orders) the plans of the appellant when they were not initially produced under disclosure procedures.

The Court concluded that theses approaches were unsatisfactory – s.5(2) (VLA), in assessing the value of the improvements, required the cost of actual improvements in place to be provided.

2. External Structures

Two very expensive structures external to the subject site – a traffic flyover and a bridge over Little Tallebudgera Creek - were constructed and paid for by the original site developer as part of the development approval. The question was whether these were improvements "appertaining to the land" (under s.6 of the VLA) and thus to be deducted in arriving at an unimproved capital value.

The Court held whether something "appertains" to land is a question of law which turns on whether the thing is question is in someway an "incident" to the ownership of the land. Whilst it was a condition of development that the flyover be constructed, that did not make it an incident of ownership. It merely placed an obligation on the landowner similar to a developer being obliged to construct a median strip, a roundabout or curbing and channelling.

The Court concluded that the flyover and the bridge costs were not improvements and should not be deducted in any exercise under s.5(2).

3. Improper Disclosure

Under the general duty of disclosure provisions (under the *Uniform Civil Procedure Rules 1999* adopted by the *Land Court Rules 2000*) there is an ongoing requirement on parties to produce to the other side any material that is directly relevant to a matter in issue in the proceedings. The question arose as to whether the appellant should have produced the "as constructed" plans at a much earlier stage of the proceedings than was actually done.

Even though there were no pleadings as such between the parties in this case, the issues had been identified to an extent from expert reports tendered or exchanged well before trial. It would have been obvious to the parties that the "as constructed" plans would have been directly relevant to the issue of replacement cost of the improvements. The Court considered that the test of direct relevance had been established. The plans were clearly of value in understanding the nature of the improvements. Even the late disclosure allowed the respondent to modify his appreciation of the improvements in certain respects. Such material should have been produced an earlier stage by the appellant.

4. Depreciation

A very detailed analysis of the proper approach to depreciation on major retail/commercial buildings is provided by the Court in this decision.

In valuing tangible improvements, the parties employed the :depreciated replacement cost" method. That method involves, first, an estimation of the replacement cost of improvements as new as at the date of valuation and, second, the deduction from the estimate of an amount to reflect any decline in value of the improvements from their value as new.

The methods of depreciation by the parties differed. The respondent employed a straight line method to depreciate for age while the appellant employed a method said to represent the loss of economic value - in effect, an adoption of a capital allowance as an indicator of depreciation. The appellant's reasoning was that this capital allowance had the effect of maintaining the rental income from the property as if it were new. The respondent's response was that, notwithstanding such expenditure, the rental income would be less than it would be if the improvements were in fact new.

Quoting *Rost and Collins* (the standard valuation text), the Court indicated that loss in value may be attributable to physical deterioration, functional obsolescence or economic obsolescence. Physical deterioration and functional obsolescence may be subdivided into curable and incurable elements. Curable elements are capable of economic restoration while incurable elements are those which cannot be restored or where the utility following the restoration would not justify the cost. Examples of functional obsolescence include: inconvenience in interior layout, outdated and inefficient lifts, fixtures and fittings which are apparent having regard to the current requirements or standards.

The Court observed that the lessening of economic utility may be caused by external circumstances. In the case of a shopping centre, the emergence, for example, of an attractive new competitor may pose a threat to an older shopping centre and therefore contribute to economic decline.

The Court was critical of the appellants approach to depreciation in that it only addressed curable physical deterioration.

As regards the respondent's approach to depreciation, the Court rejected the proposition that decline in value would have occurred in a straight line. The level of decline was seen as a market value consideration and there was no evidence that the market operated in that way throughout the life of the improvements. The Court stressed that what needed to be borne in mind was that the improvements being valued were those in existence at the date of valuation. The Court also observed that the potential for expansion and refurbishment promoted the view that the bulk of the existing structures retained a substantial value.

In the end, the Court found that the appellant's evidence concerning depreciation and value of improvements fell short in addressing curable elements only. It did not address the incurable though the appellant was thought to have had the expertise within its camp to do that. As to the respondent, it failed to lead evidence which provided any support for its straight line method a method. Any attempt by the Court to devise a depreciation rate or amount based on the evidence before it was seen to be a guess and not a practicable test as was required by law.

5. Jurisdiction of the Court

The Court ultimately rejected the exercises which the parties purported to carry out under s.3(2). The Court held that, if the state of the evidence was such that it could not be convinced that a value contended for by either party or otherwise discovered by a consideration of the evidence was correct, then it could dismiss the appeal and affirm the valuation appealed against. Equally, it was could determine the value as found by application of the s.3(1)(b) method alone.

The Court needed to be satisfied that the elements of s.3(2) were complied with; if they were not, it could not be said that that exercise is carried out correctly in accordance with the Act.

If the evidence of the assessment of "improved value" or the "improvements" was defective and the defect could not be remedied by the Court, the s.3(2) exercise could not be said to be carried out correctly.

While the Court concluded that the improved value of the subject for the purposes of s.3(2) was acceptable, it could not conclude the same as to the value of the improvements on the evidence.

The Court thus concluded that it was within its jurisdiction to reject an approach under s.3(2) and solely adopt the conclusion from a s.3(1)(b) approach. In the result, a determination of an amount of $128,200,000 was made.

3. MULTIPLEX (240 QUEEN STREET)

Multiplex 240 Queen Street (*Multiplex*) was one of five major CBD appeals heard at one combined hearing. Much of the evidence and issues were common to all cases. The Land Court handed down a separate decision in *Multiplex* first but in doing so canvassed many of the common matters. Only the *Multiplex* decision is noted here.

In *Multiplex,* the Chief Executive issued valuation was in the amount of $15,000,000. However, he had attempted to lead evidence to a much higher figure of $43,000,000 based on a s.3(2) approach. (No deduction for "intangibles" was made in arriving at this figure as a s.35(A) application had not been made by the appellant). This approach by the Chief Executive was rendered inadmissible in a preliminary hearing in *Multiplex*.

As there was a sale of the subject property (unlike the Chermside and Pacific Fair decisions where the improved value of the shopping centres was arrived at by a capitalisation of rents approach) it was held permissible to use the improved subject sale as evidence in arriving at an unimproved value of the subject. Under s.3(1)(b), using this "deduction" method, the Chief Executive's valuer arrived at a figure of $34,000,000 (including a deduction for "intangibles"). This improved sale was ultimately rejected by the Court as unreliable evidence due to the difficulty in analysing the value of the improvements.

If such a figure of $34,000,000 was not accepted, the Chief Executive put three alternatives figures, derived from direct comparisons with site sales:

- sales where the dominant use was retail. - $21,300,000
- sales where the dominant use was commercial. - $13,900,000
- sales where the dominant use was residential. - $11,700,000

The Chief Executive adopted retail use as the highest and best use for valuation purposes.

Under the Town Planning Designation (Multi-Purpose Centre – City Centre) applicable to the subject site, a wide range of activities were allowed to be clustered together. Both high-rise commercial and residential were permitted in this city centre area.

The appellants contended for a valuation of $12,860,000, at the relevant date of 01/10/2003.

In the process of arriving at this decision, the Court considered various factors including:

1. Use of improved sales

The difficulties in arriving at unimproved values from highly improved sales was strongly emphasised:

> "The difficulty and uncertainty of accurately attaining the added value of improvements on a highly improved sale property increases with the complexity and intensity of the improvements. There is such a high likelihood of error in such analysis even the most competent valuer can have little confidence in the unimproved value arrived at by that process."

These difficulties are compounded where a s.3(2) exercise was performed as the improved value in those circumstances was usually established by a means other than the sale of the subject land such as capitalisation of net income. In such circumstances, not only was there the difficulty in estimating the added value of the improvements but in arriving at the improved value to commence with. Establishing the appropriate net income and capitalisation were often fraught with difficulty.

2. Valuation of Investment Properties – Novel Approach

The Chief Executive's valuer (Mr Mark Denman) proposed a somewhat novel approach for the valuation of improved investment properties (e.g., shopping centres or commercial office developments). Mr Denman argued that for these investment properties the use of unimproved or lightly improved sales as a basis for such valuations was inappropriate. He maintained that it was only by the analysis of highly improved sales (or if s.3(2) method of valuation was admissible by the deduction of the value of improvements from the deduced improved value of each parcel of land) that the true unimproved value of the land could be ascertained.

For the subject land Mr Denman attempted to apply his theory by the analysis of the sale of the subject land and also by comparison with the unimproved values derived from sales of other improved commercial properties.

What was considered revolutionary by the Court about Mr Denman's theory was the extent to which it is asserted that certain elements of value (principally profit and risk or entrepreneurial profit) remain embedded in the unimproved value.

Because of the Court's ultimate rejection of both valuers analysis of improved commercial sales, the validity or otherwise of Mr Denman's theory was not required to be determined. However, the Court did make the following observation:

> "He asserts that vacant land sales do not truly identify the value of the land component of improved land because there will be an erroneously lower level of value from such sales, which have never been put to their unfulfilled potential and associated development risks. If that is correct, that method, together with the s.3(2) method which also includes the "embedded value" of the profit and risk component, will always result in a higher unimproved value than one based on vacant land sales. I cannot accept that, at least as far as CBD properties are concerned."

3. Residential Potential and the *QNI* case

Mr Jackson, the appellant's valuer, argued the subject could not have potential for residential development because of the *QNI* decision. The Court held that Mr Jackson misunderstood the application of this case. The Court's view of the *QNI* principle was that as follows:

> "If it can be demonstrated that the subject land is improved land, that is the structures and other works on the land add value to the land, s.3(1)(b) requires that those improvements be notionally removed and the land is then to be valued as if the improvements did not exist. In this case there was agreement that the buildings added value to the appeal lands. In the Court's view Mr Jackson was not correct in excluding any residential potential for the subject land simply because the cost of demolition of the existing improvements would be prohibitive."

4. Scarcity Premium

In the absence of any evidence of a scarcity premium (as discussed in the High Court *Maurici* decision) for unimproved site sales, the Court accepted that no such premium should be applied.

5. Commercial Sales

Ultimately there was only one sale in this category of sufficient comparative worth, namely 6 Queen Street Brisbane (Brisbane Plaza). A sale from for $28,028,000 from Suncorp to ABN Amro was used by both valuers but their analysis and comparisons were quite different. There were two main points of difference:

- whether the sales should be analysed over the entire site, including the public plaza area or over the area to be developed as such.

- whether the sale should be discounted for pre-commitments, ("agreements to lease" of major tenants) and development approval.

Site Area or Development Area

The Court held the analysis of the site should be over the entire area – the development approval was over the whole area and required an area for plaza public open space; set backs were required for the protection of the heritage Treasury building; further, there was a car park under the public open space area.

Agreements for Lease and Development Approval

The development approval and "agreements for lease" were steps taken in realising the development potential of their land and in that sense added value to it. The agreements for lease were not a lease as such nor an improvement on the land. The sale price should not be discounted for the agreements for lease – such merely indicated the degree of ripeness of the sale property for the redevelopment. The development approval was held to attach to the land and run with the land itself. Regard can be had to the successful development of the subject as a commercial investment property. The ripeness of the subject property and sale were considered similar.

6. Theory of Merged Markets

The issue here was whether residential sales were of any relevance in determining the unimproved value of the subject with an highest and best use as commercial; that

depended on whether there were separate and distinct markets for residential and commercial. The Court concluded that, as at the relevant date, purchasers of development sites in the CBD, whether for commercial or residential purposes, were competing in the same market. Each site would then be developed in the manner which would provide the developer with the maximum return, regardless of whether that be retail, commercial or residential. The Court referred to the Felix development and the Riparian development (with significant residential component) to show residential development was actively pursued in the main commercial office areas of the CBD.

7. **Deferred Settlement of Sales**

Where there had been deferred settlement of sales, Mr Jackson discounted the sale prices to adjust them to the prices they would have achieved on a cash sale basis. In his opinion a cash sale would be on a 10% deposit with settlement of the sale within 60-90 days. Where there was a deposit of less than 10% or settlement exceeded 90 days, he discounted the sale price to recognise the departure from normal terms.

The Court held that the principle relied on by Mr Jackson in making those adjustments was well established. Where it can be demonstrated that a sale price was increased to account for the period between contract and settlement an adjustment should be made. However, where there is no evidence that the sale price was increased because of a delayed settlement, it would be wrong to assume that the sale price negotiated between the parties contained a component for the settlement period. In many cases, a vendor may be prepared to accept the delay, secure in the knowledge that the purchaser was locked into a fixed price, whether the market rose or fell.

8. **Presumption of Correctness** - Section 33

The combined evidence of both valuers clearly showed that the valuation of $15,000,000 could not be sustained. The Chief Executive could not therefore rely on the presumption of correctness. The issued value was required to be set aside and another one substituted.

9. **Relevant Evidence**

The Court found that the highest and best use of the subject land to be commercial. The best evidence was found to be the commercial sale of 6 Queen Street and certain other more recent residential sales.

6 Queen Street was found difficult to compare with the subject land. That property was a large site in a very prominent location with four street frontages, (an island site), with uninterrupted views, an aspect over the Brisbane River with the mall at the southern end and directly opposite the low rise Heritage Treasury Casino which afforded protection to its views and natural light. However, because of its location the subject land was considered superior on a pro-rata basis.

Later residential sales including Festival Towers and Vision Tower showed the market for residential as at 1 October 2003 was approaching $5,000 per m² for sites, some distance removed from the Mall. There was no dispute between the valuers that

the market for well located commercial land was higher than the market for similarly located residential land. It could therefore be assumed that the market for the subject lands, a prime corner site in the commercial precinct adjacent to the Mall must be substantially higher.

Determination

The Court determined the value of the subject land at $6,300 per m² or $13,400,000; approximately $475 per m² net lettable area.

4. PERPETUAL TRUSTEE (CREDIT UNION HOUSE)

The Land Court decision in this matter was noted in last year's review. An appeal to the Land Appeal Court was dismissed but that decision is of interest on three issues. Some brief background is first necessary. This case concerned the unimproved value of the site of Credit Union House (175 Eagle Street) an L-shaped lot fronting the Brisbane River and adjacent to the historic Customs House. Two thirds of the site accommodated a 20-story commercial building whilst the remainder (southern section) contained a subterranean parking area and light and air easements in favour of adjoining 167 Eagle Street. Between the car park area and easement area was a volumetric lot of some five storeys high, having separate title which could be developed for river front units or the like.

The three issues to note are:

1. Should a premium be placed on the subject's value because of its river frontage and, if so, how should it be assessed?

2. How should the impediments to the southern part of the site, that is, light and air easements and the volumetric lot be assessed. How should any advantage given to the balance of the site be addressed?.

3. Should the unimproved value of the components parts of the southern site - the subterranean car parking area, the volumetric lot and the open impeded space above – equal the single site value.

The Court held:

1. River front Premium

As well as river frontage, the northern section of the subject had the benefit of unrestricted river views directly across the river to the north and south.

There was no rental evidence to support a 20% premium for river frontland. As to sales, there was evidence that the river front Riparian site (with other disadvantages) showed a greater premium over non river front Aurora and Felix, demonstrating that a significant premium was paid for a site with riverside location. Also, there was evidence that apartments with bridge/river views attracted a premium of 20%. River views were restricted or not available from Aurora and Felix from the lower floors.

It was also noted that river views available from the subject could not be built out, a characteristic directly related to river views. A premium was justified despite river advantage offset somewhat by difficulties with construction. Allowance was also made in calculating the premium for the distinction between residential and commercial sales. In the result, a 20% premium applied to the northern section of the site was maintained.

2. Easement Impediments

The Land Court assessed the value of the southern area of the subject by applying a discount of 45% to the assessed value of the northern portion. The Land Court found that, but for the two impediments, the southern area would as part of the whole have the same value as the northern area. The Land Court valued the northern portion as if it were part of an overall site without impediments of the type found on the southern area. The Land Appeal Court accepted the approach of discounting that figure to allow for impediments rather than attempt to value the southern portion on a stand alone basis.

There was little evidence to suggest that the development of the site as a whole had been significantly affected by impediments. Easements (light and air) may have limited the development options by restricting the location of a building (as with the Riparian site) but the development capabilities of the subject site remained the same.

Retention of the southern area in a largely undeveloped state enabled the northern portion to be developed with a building with river views to the south which could not be obstructed and which had the light and air benefits flowing from the south. The southern portion also provided the underground car park and superior access to the site.

Thus, the southern area with the impediments in place played a substantial role in the maintenance of the value as a whole. That conclusion did not involve a double counting but rather a recognition of the benefits which remained after the excision of the volumetric lot and the grant of easements for light and air.

3. Value of Component Parts

The appellant argued that the sale value of volumetric lot should be taken into account when assessing the value of the southern portion.

The Court held that the volumetric lot was a separate lot which, because of its limited height, appeared to have a completely different use from the subject and sites such as Riparian. In those circumstances, it could not be assumed, in the absence of evidence, that the value of the separate parts of the southern - area the volumetric lot, the underground car park area, and the air space subject to easements - would equal the value of the whole.

5. SURFERS PARADISE BEACH RESORT (Q1)

Q1, described as the World's tallest residential tower, was referred to the Land Court for determination of its unimproved value (as at 2003 and 2004). At the outset, it is of interest to note some of the features of the site and the building situated thereon. The site, made up of 18 separate lots before amalgamation in 2004, comprises an area of 12,660 m², occupies almost an entire block some 400 metres south of Cavill Avenue, Surfers Paradise and is one block back from the beach.

Development of an 80 level tower was completed in October 2005. This comprises 972 bedrooms, two levels of basement car parking, a two level observation deck, retail shops on the ground floor, a health club and conference facilities. Approvals allowed 94,931m² GFA (not including the observation deck), a plot ratio of 7.5:1 and a bedroom ration of 13:1.

Under the *Gold Coast Planning Scheme 2004*, the Precinct 1 in which Q1 was located, had no restrictions on building height, residential density or GFA ratio.

The departmental valuers (Mr Phil Smith and Mr Ian Hawley) placed valuation of $44,000,000 for October 2003 and 2004. Mr Grant Jackson, for the appellant, submitted a valuation for these periods of $31,600,000.

Key Issues

The key issues before the Court were:

- Whether three older improved sales in Surfers Paradise could be used in the valuation of the subject.
- The market comparability of Surfers Paradise and Broadbeach and whether the sales in Broadbeach could be used to value the subject.
- The appropriate valuation methodology.

Mr Jackson argued Broadbeach to be in an entirely different environment to Surfers Paradise, appealing to a different, more elegant market of older permanent residents. Surfers Paradise, he argued, more related to tourism and aimed at younger people with entertainment, clubs and 24-hour activity. There was quite different level of development at Surfers Paradise with many high-rise constructions compared with Broadbeach.

The Departmental valuers considered Surfers Paradise and Broadbeach directly comparable and, with an absence of recent sales in Surfers Paradise, Broadbeach was seen as the next logical place to look for evidence.

There was limited sales activity in the Surfers Paradise after October 2003 whereas all Broadbeach sites were sold between October 2003 and October 2004. The developers turned to Broadbeach as Surfers Paradise sites had dried up.

The Court held:

1. The subject site was unique amongst the properties under consideration because of its size and location on the southern fringes of the Surfers Paradise Precinct 1.

2. As to the differences between Surfers Paradise and Broadbeach, Surfers Paradise was seem to have a superior development potential with Broadbeach a quieter residential locality.

3. There was sufficient difference between Broadbeach and Surfers Paradise to indicate the Broadbeach sales should not be used directly in valuing the subject. They could only be used to show the upper limits of the subject's valuation.

4. The Surfers Paradise sales contemporaneous with the dates of valuation provided the most reliable evidence of the value of the subject (Artique, Avalon and Mercure).

5. Earlier improved Surfers Paradise sales (Raptis Plaza, Dolphin Arcade, and Circle on Cavill) showed values lower than the subject. But there was no evidence of the quantum of rise in the market between these sales and the relevant date. Therefore, there was no obvious way adjustments could be made; the weight of such sales was thus decreased.

6. The Broadbeach sales of the Oracle and, to a lesser extent Pegasus and Sierra Grande, showed values higher than the subject. There was no limitation in principle on using a series of individual sales (as occurred in some of these developments) to find an amalgamated value, even if such sales occurred over a period of years.

7. The rate per m² provided a consistent basis for comparison – but also taking into account differences: as of right height restrictions, GFA ratio and bedroom density. A rate of $3,000 per m² was applied to the subject – analysing to $39,917 per bedroom and $408 per m² GFA. These figures were seen as consistent with the sales evidence relied on.

6. SORRENTO

The decision of the Land Appeal Court in this matter (confirming the Land Court decision) was noted in last years Review. Since then, the resumee Sorrento has successfully appealed to the Court of Appeal.

Background

Sorrento was the lessee of a section of a building on land, part of which was resumed for road widening purposes. The resumed land comprised part of a car park adjacent to the building. Sorrento had no separate leasing rights to the resumed area but two clauses in the building lease gave it certain rights to use the resumed car park area.

The principal issue for the Court was whether the rights granted to Sorrento amounted to an "estate or interest" under s.12(5) of the *Acquisition of Land Act* (ALA) sufficient to found a compensation claim.

One of the lease clauses gave Sorrento exclusive rights to use two car parking spaces for doctor's parking; a second clause gave Sorrento rights to use the remaining on a non-exclusive basis for patient parking.

The Land Court and the Land Appeal Court held that the rights to use the resumed area granted to Sorrento under the lease clauses did not constitute a lease and thus did not come within the term "estate or interest" under s.12(5).

Decision

In allowing the appeal, the Court of Appeal (by majority, Holmes JA dissenting) held that:

- The basic issue before the Court was really one of the statutory construction of s.12(5) of the *Acquisition of Land Act*

- "Interest" in the s.12(5) has the same meaning as defined in the *Acts Interpretation Act 1954* (Qld) s.36 and that includes a "right, power or privilege over or in relation to the land".

- The appellant did not have an interest in land as that phrase has been construed at common law.

- The appellant's licence to use the car parking spaces was an "interest" because it was a contractual right and a right of property.

- The right to car parking was valuable not only from a commercial point of view but also because local government regulations required the medical centre to have sufficient off street parking.

- Section 12(5) will only apply to allow compensation in situations where literal interpretation of "interest" does not produce an absurd result. For

example, picnickers who go on public land would be excluded from the class of those who may properly claim compensation if such land is resumed.

- Applicable here was the High Court observation in *Marshall* (2001) that statutory provisions [like s.12(5)] conferring a right to compensation where land is resumed for public benefit should be construed with all the generality that the words permit.

Main Roads Department have now sought special leave to appeal this Court of Appeal decision to the High Court. While the amount of any compensation at stake may be relatively small, the purpose of the appeal would seem to be to clarify the types of interest that are properly claimable.

7. EDGARANGE

The principal issue in this case was whether the claimant's right to compensation was limited because the relevant scheme of resumption also gave rise to a statutory entitlement to compensation under the *Integrated Planning Act* (IPA). Put another way, did the so-called "Point Gourde in reverse" principle apply.

The claimant's resumed land would probably have been approved for industrial development had not the Redland Shire Planning Scheme been altered to accommodate the proposed resumption for road works and sewerage treatment purposes.

The respondent Council's argument was founded on the basis of the claimant having a "prior right to compensation". It argued that this case raised for consideration the question as to the interrelationship between the compensation provisions of the *Acquisition of Land Act* (ALA), the compensation provisions of IPA and the common law principle of "Point Gourde in reverse".

It submitted that the interrelationship should be resolved as follows:

> "When assessing the compensation payable and consequence of the compulsory acquisition of an interest in land, the common law principle for which *Melwood Units* is authority does not apply where the market value of that interest has been depreciated by a scheme of resumption, in circumstances in which the existence of that scheme also confers a statutory entitlement to compensation on the owner of the interest."

The claimant's response was two-fold: first, as a consequence of the compulsory taking of its land, the claimant has a statutory right to claim and have assessed compensation pursuant to the ALA. Second, the common law principle enunciated in the *Crown v Murphy* is part of the law governing the proper assessment of compensation for purposes of the ALA and as such could have only been displaced or ignored where clear legislative justification to do so existed.

The Court held that:

- the operation of the relevant common law principle contended for by the respondent was not to be found in any of the cases referred to. Nor is it to be found either by in express terms or by necessary implication in the application IPA or ALA.

- relevant here was the important statement of principle in *Marshall* (2001) by the High Court that statutory provisions conferring a right of compensation for resumption should be construed with all the generality that their words permit.

- to accept the respondent's argument would require the introduction of a limitation or qualification to the operation of s.20 of ALA which was not found in the terms of the statute.

- on the respondent's argument, it was concerned that that there may be two pieces of litigation in two separate Courts rising out of the one resumption. That is, in some compulsory acquisition cases involving town planning schemes introduced in the furtherance of a resumption, the landowner might be required to recover compensation for injurious affection arising out the changes in zoning from the Planning and Environment Court and compensation, under various heads identified in s.20 of ALA, from the Land Court.

- it acknowledged that rejection of the respondent's argument could in certain circumstances raise the potential for duplication in the assessment of compensation under ALA and IPA. However, it held such circumstances should be rare and the Land Court and the P & E Court would be vigilant to avoid such duplication.

8. LAMB

In *Lamb* the Court of Appeal had to consider the validity of the process under which the Brisbane City Council listed property in its Heritage Register. The existing process was to include a specific property as part of a planning policy as opposed to an amendment to the planning scheme itself. Such procedure was far less complicated, time-consuming and costly that an amendment to the planning scheme. (Although an owner could still provide reasons to the Council against heritage listing).

Prior to its heritage listing, the demolition, removal or relocation of the subject residence at 81 Dornoch Terrace Highgate Hill was "exempt" from the need for permit under the Town Plan. With heritage listing, the property became "impact assessable" with a development permit necessary for such action. Rights of submission and appeal then arose in members of the wider public.

Under the *Integrated Planning Act 1997* (IPA), it was provided that a planning policy could not regulate development or the use of premises. The issue for the Court of Appeal was really a question of statutory construction of IPA. Specifically, was the heritage listing planning policy sufficiently incorporated into the wider planning scheme so as not to offend the statutory prohibition. Overruling the Planning and Environment Court, the Court of Appeal found that the heritage listing policy and wider planning scheme worked in tandem - the planning scheme was the sole source of regulation, adopting the policy rather than the other way around. In short, the Court of Appeal found the heritage register planning policy to be valid.

When a property is heritage listed under Council provisions, an owner is given two years (under IPA) to lodge a Development Application (Superseded Planning Scheme) (DASPS) which, if refused, can lead to a claim for compensation for loss of development rights occasioned by the listing. In the instant case, the such Development Application was lodged slightly outside the two year period.

The Court of Appeal held that it was not legally open to invoke the discretion of the Court to extend such time. The lodging of a DASPS was not a requirement under IPA which could be varied; but if it was lodged, the time limit must be complied with strictly.

The Court of Appeal noted that it was not surprising that the making of applications of this kind should be confined by legislation to a time limit which could not be extended by the subsequent Court discretion. There was a need to draw a line beyond which superseded planning schemes ceased to be relevant to the life of a community.

If it is of interest to note that there is no compensation provision provided for heritage listing under the State Heritage Legislation (1992). It is clearly within the power of a State Parliament to take such a policy decision.

Table of Cases

1. PT Limited v Department of Natural Resources and Mines [2006] QLC 0068 *****
2. Kent Street Pty Ltd & ors v Department of Natural Resources and Mines [2006] QLC 0111 *****
3. Multiplex 240 Queen Street Landowner Pty Ltd v Department of Natural Resources, Mines and Water [2007] QLC 0010 *****
4. Perpetual Trustee Company Limited v Department of Natural Resources, Mines and Water [2007] QLAC 0025
5. Surfers Paradise Beach Resort Pty Ltd v Department of Natural Resources, Mines and Water [2006] QLC 0072
6. Sorrento Medical Services Pty Ltd v Chief Executive, Department of Natural Resources, Mines and Water [2007] QCA 0073 ******
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****** Under Appeal to High Court